No. 90-279

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

HORACE D. McCOWAN, JR. and
SARAH E. McCOWAN,

Petitioners,

vs.

SEARS, ROEBUCK AND CO., and
DEAN WITTER REYNOLDS, INC.,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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QUESTIONS PRESENTED FOR REVIEW

1. Whether the United States Court of Appeals for the Second Circuit erred by waiving jurisdictional requirements of Rules 3(c) and 4(a) of the Federal Rules of Appellate Procedure and, on its own motion, exercising "pendent appellate jurisdiction" over a nonappealing party and reviewing an unappealed, but otherwise appealable judgment order?

2. Whether "pendent appellate jurisdiction" attaches to an interlocutory appeal under 9 U.S.C. § 15(a)(1)(A)?

3. Whether a mandatory stay for arbitration may issue pursuant to 9 U.S.C. § 3, absent an agreement in writing for the arbitration of a claim then pending in a federal court against a party before the court?

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PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

THE PARTIES TO THE PROCEEDINGS BELOW

Horace D. McCowan, Jr. and Sarah E. McCowan (hereinafter "plaintiffs") petition for a writ of certiorari to review a judgment of the United States Court of Appeals for the Second Circuit. The caption of this case in this Court contains the names of all other parties.

OPINIONS BELOW

The proceedings below arose from a consolidated appeal of two orders of the United States District Court for the Southern District of New York. The first order was entered on October 5, 1989, and the district court's opinion (A-39)[1] is reported at 722 F. Supp. 1069 (S.D.N.Y. 1989). The second order was entered on January 17, 1990, and the district court's opinion (A-56) is reported at 1990 W.L. 4024 (S.D.N.Y. 1990). The opinion of the circuit court of appeals (A-1) is not yet reported.

GROUNDS OF JURISDICTION

The United States Court of Appeals for the Second Circuit entered the order sought to be reviewed on May 25, 1990 (A-1), and this petition is filed within ninety days of entry of that order. *See* 28 U.S.C. § 2101(c) (1982). This Court has jurisdiction to review the judgment in question by writ of certiorari pursuant to 28 U.S.C. § 1254(1) (1988).

STATUTES INVOLVED

This petition involves Rules 3(c) and 4(a) of the Federal Rules of Appellate Procedure (A-84); Sections 3 and 15 of the United States Arbitration Act (the "Arbitration Act") (A-86), 9 U.S.C. § 3 (1970) and 9 U.S.C. § 15 (1988); Sections 502 and 522 of the Virginia Securities Act (A-87, 88), Va. Code Ann. § 13.1-502 (1956) and Va. Code Ann. § 13.1-522 (1956) (amended 1987), and Rules 8(a) and 19(a) of the Federal Rules of Civil Procedure (A-89). The pertinent text of each provision is printed in the appendix.

STATEMENT OF THE CASE

On December 31, 1986, plaintiffs filed a complaint (A-61) against Sears, Roebuck and Co. ("Sears") and Dean Witter Reynolds Inc. ("Dean Witter") in the United States District Court

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[1] "(A-____)" refers to pages in the annexed appendix. All emphasis is added.

for the Eastern District of Virginia asserting a claim against Sears for violations of Section 522 of the Virginia Securities Act allegedly occurring while Sears was in control of Dean Witter. The basis for federal jurisdiction in the court of first instance is 28 U.S.C. §§ 1332, 1391(a) (1976). Although Dean Witter is a named defendant, the complaint expressly demands a "judgment against the defendant Sears, only" (A-67) and asserts no claim for relief against Dean Witter, the latter having been included as a party defendant only because of Rule 19(a) of the Federal Rules of Civil Procedure. (A-89).

On defendants' motion, this action was removed to the United States District Court for the Southern District of New York.[2]

Plaintiffs have entered into an agreement with Dean Witter providing, in material part, that any controversy between plaintiffs and Dean Witter arising out of or relating to that agreement or the breach thereof shall be a subject of arbitration (A-75-76, ¶ 16). Although plaintiffs have no agreement with Sears for the arbitration of any claims against Dean Witter, both Sears and Dean Witter moved for a stay pending arbitration of plaintiffs' claims against Dean Witter.

By its order entered on October 5, 1989, *inter alia*, the district court denied Sears' and Dean Witter's several motions for a stay pending arbitration of plaintiffs' claims against Dean Witter. (A-39, 53).

On November 6, 1989, Dean Witter filed its only notice of appeal herein, expressly appealing "from the Order entered in this action on October 5, 1989." (A-68). Statutory jurisdiction of the Dean Witter appeal was founded solely on 9 U.S.C. § 15(a)(1)(A), providing for the interlocutory appeal of an order denying a mandatory stay under 9 U.S.C. § 3. Sears filed no notice of appeal from the order of October 5, 1989.

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[2] In the Southern District this action (the "Sears Action") was consolidated for pre-trial proceedings with plaintiffs' action against Dean Witter (the "Dean Witter Action") on federal law claims under the Securities Act, the Securities Exchange Act, and RICO then pending in that court. Thereafter, the Dean Witter Action was stayed pending arbitration.

On November 16, 1989, Sears alone moved (A-70) the district court for a mandatory stay of all proceedings "as against Sears, Roebuck and Co. pending arbitration of the claims against Sears, Roebuck and Co." (A-71). Neither Sears nor Dean Witter has an agreement with plaintiffs for the arbitration of any claims against Sears.

By its order entered on January 17, 1990 (A-60), the district court denied Sears' motion.

On January 24, 1990, Sears filed its notice of appeal in this action, expressly appealing only "from the Order entered in this action on January 17, 1990" — the order denying a mandatory stay pending arbitration of plaintiffs' claims against Sears. (A-82). Statutory jurisdiction of the Sears appeal also was founded solely on 9 U.S.C. § 15(a)(1)(A), and Dean Witter filed no notice of appeal from the order of January 17, 1990.

After consolidating the Dean Witter appeal from the order of October 5, 1989 with the Sears appeal from the order of January 17, 1990, the Second Circuit issued one judgment and final opinion (A-1).[3] The court of appeals concluded that Dean Witter's notice of appeal of November 6 was ineffective under Rule 4(a)(4) of the Federal Rules of Appellate Procedure, since Dean Witter's notice of appeal had been filed before the district court entered its judgment order disposing of Dean Witter's Rule 59 motion.

Although the Second Circuit concluded that Dean Witter had filed no effective notice of appeal, the court assumed jurisdiction over Dean Witter and its appeal from the order of October

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[3] At first the Second Circuit went outside the record and issued an opinion (A-21), reported at ____F.2d____, 1990 W.L. 101117 (May 25, 1990), resting jurisdiction of the Dean Witter appeal entirely on an informal "announcement" of the district court's ruling (A-54) on Dean Witter's post-judgment motion — an announcement reportedly made *ex parte* by the district judge's law clerk exclusively to counsel for Dean Witter, and first disclosed by Dean Witter in its reply brief in the Second Circuit. This opinion was amended, however, on July 10, 1990, after consideration of this Court's holding in *Acosta v. Louisiana Dep't of Health and Human Resources*, 478 U.S. 251 (1986). (A-1).

5, 1989, reversed the district court's order of October 5, 1989, granted a "stay as to Dean Witter" (A-20), and declared that all "claims against Dean Witter must be stayed pending arbitration under section 3 of the Arbitration Act". (A-19).

The court of appeals considered only "the district court's denial of Dean Witter's stay" (A-13), took no direct action on Sears' appeal, and declined to "determine" whether the district court's order of January 17, 1990, had properly denied Sears a mandatory stay (A-20). Having granted a stay to Dean Witter, however, the court simply declared, *sua sponte*, that "the suit against Sears . . . cannot proceed." (A-20).

REASONS FOR ALLOWING THE WRIT

This Court Should Grant Certiorari to Review a Decision that Expands "Pendent Appellate Jurisdiction" to Encompass an Unappealed, but Otherwise Appealable Judgment, Extends Appellate Jurisdiction to a Nonappealing Party, and Sanctions Compelled Arbitration Other than as Agreed by the Parties, All Contrary to the Usual Course of Judicial Proceedings and in Conflict with this Court's Decisions in *Torres*, *Abney*, *Volt*, and *Moses H. Cone*.

In material part, the Virginia Securities Act expressly provides that any person controlling a person selling securities in violation of that act "shall also be liable . . . severally with and to the same extent" as such seller, unless such controlling person demonstrates that it could not have known of such violation through an exercise of reasonable care. *See* Va. Code Ann. § 13.1-522(b) (A-88).

Here, plaintiffs have asserted only this separate, several liability of Sears. As the district court noted, "this case is between the plaintiffs and Sears". (A-55). Although plaintiffs also have very real state law claims against Dean Witter under the Virginia Securities Act, and although there may exist a potentially "arbitrable 'controversy' " (A-17) between plaintiffs and Dean Witter for Dean Witter's violations of the Virginia Securities Act,

plaintiffs have not pursued[4] this potentially arbitrable controversy or asserted these state law claims against Dean Witter, at some obvious risk to plaintiffs.

Dean Witter is named as a party defendant in plaintiffs' action against Sears because, as the district court held (A-5), Rule 19(a) of the Federal Rules of Civil Procedure required Dean Witter's joinder, as one claiming an "interest relating to the subject of the action" that might be prejudiced without such joinder.

The court of appeals declares, however, that plaintiffs' claims asserted against Sears under the Virginia Securities Act are actually "claims against Dean Witter." (A-19). The court then summarily stops all proceedings in this action against Sears, and, using Dean Witter's arbitration agreement, decrees that "Dean Witter is entitled to a mandatory section 3 stay", that the "claims against Dean Witter must be stayed pending arbitration under Section 3 of the Arbitration Act", and that "the suit against Sears . . . cannot proceed" pending such arbitration. (A-19-20).

In short, all proceedings in this action against Sears are stopped solely because Dean Witter (not Sears) "is entitled to a mandatory section 3 stay" pending the arbitration of all "claims against Dean Witter" (A-19-20), although such claims are not in issue, although Dean Witter has not appealed the order of October 5, 1989, denying such a stay, and although Sears, the only appellant before the court, has neither appealed that order nor requested such a stay.

Rule 3(c) of the Federal Rules of Appellate Procedure expressly requires that a notice of appeal specify the party or parties taking an appeal. (A-84). A party's failure to file a timely notice of appeal is a "jurisdictional bar to the appeal" and may not be waived by an appeals court. *Torres* v. *Oakland Scavenger Co.*, 487 U.S. 312, 314 (1988); *see Board of Governors v. Akins*,

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[4] Rule 8(a) of the Federal Rules of Civil Procedure expressly requires that a claim for relief must include "(3) a demand for judgment for the relief the pleader seeks." (A-89). Plaintiffs' complaint expressly declares that plaintiffs "demand judgment against the defendant Sears, only" (A-67), ensuring that no claim for relief is or can be asserted against Dean Witter in this action.

109 S.Ct. 299, 300 (1988) (vacating circuit court decision and remanding "for further consideration in light of Torres"); *United States v. City of Chicago*, 870 F.2d 1256, 1258 (7th Cir. 1989).

No notice of appeal herein specifies Dean Witter as an appellant. Accordingly, the Second Circuit had no statutory jurisdiction to grant "review of the district court's denial of Dean Witter's stay" (A-13), to reverse the order of October 5, 1989, or to issue a mandatory stay to Dean Witter pending arbitration of any claims against Dean Witter. Sears' notice of appeal did not create jurisdiction over Dean Witter or any order affecting Dean Witter, and nothing authorizes the Second Circuit to grant relief to Dean Witter, an absent party, on an unappealed issue. *See Abney v. United States*, 431 U.S. 651, 663 (1977); *Stockstill v. Petty Ray Geophysical*, 888 F.2d 1493, 1497 (5th Cir. 1989) ("requirements of Rules 3 and 4 must be satisfied as to each party" appellant); *Bonitz v. Fair*, 804 F.2d 164, 173 (1st Cir. 1986), *overruled on other grounds*, *Unwin v. Campbell*, 863 F.2d 124 (1st Cir. 1988).

The Second Circuit, however, claimed a right to exercise discretionary "pendent party jurisdiction" (A-12) over Dean Witter and its appeal. But whatever the concept of "pendent party jurisdiction" may encompass,[5] it can create no jurisdiction for Dean Witter. *Torres*, 487 U.S. at 317.

Also, whatever its scope, pendent appellate jurisdiction is to be exercised sparingly, and then only to permit review of an otherwise nonappealable order at the request of an appealing party. *See Akerman v. Oryx Communications, Inc.*, 810 F.2d 336, 339 (2d Cir. 1987); *Barrett v. United States*, 798 F.2d 565, 571 (2d Cir. 1986); *General Motors Corp. v. City of New York*, 501 F.2d 639, 648 (2d Cir. 1974). Here, no one has sought review of an otherwise nonappealable interlocutory order.

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[5] Generally, "pendent party jurisdiction" has referred only to an extension of federal jurisdiction to an adjudication of claims against parties with no independent basis for federal jurisdiction. *See, e.g., Finley v. United States*, 109 S. Ct. 2003, 2008 (1989); *United Mine Workers v. Gibbs*, 383 U.S. 715 (1966).

The court simply has exercised jurisdiction over an otherwise appealable judgment order. No exercise of "pendent jurisdiction" is needed to review such an order. If Dean Witter had properly noticed an appeal of the judgment order of October 5, 1989, it would have succeeded instantly. *See* 9 U.S.C. § 15(a)(1)(A).

Also, no one asked the Second Circuit to review the judgment order of October 5, 1989. Dean Witter was not before the court, and Sears, the only appellant, never requested any review of that order and never sought a mandatory stay pending arbitration of any claims against Dean Witter,[6] the only relief granted by the Second Circuit.

Under the rubric of "pendent appellate jurisdiction" the Second Circuit simply has decided Dean Witter's appeal using Sears' notice of appeal and Dean Witter's agreement. Nothing decided by the court concerns Sears' appeal from the order of January 17, 1990, and Sears' right to a stay is never determined. (A-20).

Moreover, Dean Witter's potential right to a stay has nothing to do with Sears' right to a stay, the only issue on appeal. If Sears has an applicable, written arbitration agreement, Sears was entitled to a stay. If Dean Witter has an applicable, written arbitration agreement, Dean Witter also was entitled to a stay. These two issues are totally independent if not exclusive of each other. To declare that they "overlap substantially" (A-13) as the justification for an exercise of discretionary appellate jurisdiction over Dean Witter is unfounded. Sears' appeal of the order of January 17, 1990, entails no consideration of the order of October 5, 1989, or of Dean Witter's right to a stay. The Second Circuit's confusion is most obvious in its declaration that the "appropriateness of a stay for either party requires examination of . . . the basis upon which the plaintiffs assert liability against *them*." (A-13). No such examination is required, because no liability has ever been asserted against *them*.

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[6] Any such request by Sears would have been for a "discretionary" stay, would not have been within the scope of 9 U.S.C. § 3, and, therefore, would not have been appealable under 9 U.S.C. § 15(a)(1)(A) in any event.

Even if jurisdiction had existed, however, neither defendant was entitled to a mandatory stay. A mandatory section 3 stay is authorized only when a "suit or proceeding" has been "brought" in a federal court on an issue "referable to arbitration under" "an agreement in writing for such arbitration". 9 U.S.C. § 3. Here, there is no such suit or proceeding and no such agreement.

Even if there is a latent "arbitrable 'controversy' " (A-17) over plaintiffs' dormant claims against Dean Witter under the Virginia Securities Act, that controversy is not now the subject of any claim asserted against Dean Witter in a federal "suit or proceeding", either here or elsewhere. Even if properly denominated a "claim against Dean Witter," the only claims in suit are against Sears alone.

The fact that plaintiffs could have brought arbitrable state law claims against Dean Witter in a federal "suit or proceeding" should not obscure the fact that they did not do so. Without such a suit or proceeding in federal court asserting such abeyant claims against Dean Witter, section 3 of the Arbitration Act may not be invoked by Dean Witter. *See Volt Information Sciences, Inc. v. Stanford Univ.*, 109 S. Ct. 1248, 1254 n. 6 (1989) (section 3 of the Arbitration Act "by [its] terms appear[s] to apply only to proceedings in federal court"); *Southland Corp. v. Keating*, 465 U.S. 1, 16 n. 10 (1984); *Bernhardt v. Polygraphic Company of America, Inc.*, 350 U.S. 198, 200, 203 (1956); *Shanferoke Coal and Supply Corp. v. Westchester Service Corp.*, 293 U.S. 449 (1935).

Moreover, Sears has no "agreement in writing" with plaintiffs calling for the arbitration of anything, and Sears has never asked for a stay of this action pending the arbitration of any claims against Dean Witter. Sears has requested only a stay of this action "as against Sears, Roebuck and Co. pending arbitration of the claims against Sears, Roebuck and Co." (A-71).

The Second Circuit found (A-18) that the existence of arbitrable federal law claims against Dean Witter *in the Dean Witter Action* "weighs heavily in favor of a stay of the state law claims" in this, the Sears Action. Then, after a cursory analysis

(A-18-19), the court announces that the "preclusive effect" of this litigation on the arbitration of federal claims pending in the Dean Witter Action "is potentially substantial and significant". This concern is misplaced. Whatever interest the Second Circuit may have in any such potential, preclusive effect, "the formulation of collateral-estoppel rules affords adequate protection to that interest," and "unnecessarily contorted procedures" are neither warranted nor justifiable in the name of "preclusive effect." *Dean Witter Reynolds Inc. v. Byrd*, 470 U.S. 213, 222 (1985).

The court of appeals avowedly acted in order to preserve "Dean Witter's right to arbitrate the federal claims already referred to arbitration" (A-18) in the Dean Witter Action.In so doing, the court went beyond the scope of section 3, which authorizes a stay only in aid of agreed arbitration of "the issue involved in [the] suit or proceeding" then before the court (A-86). No "federal claims" against Dean Witter are in issue here. The only issue in this proceeding is Sears' liability under the Virginia Securities Act. Solely on its own motion, the court has granted Dean Witter a discretionary stay of the state law claims asserted against Sears in the Sears Action in aid of arbitration of the federal claims asserted against Dean Witter in the Dean Witter Action, exceeding the scope of section 3 and any issue appealed or appealable by either Sears or Dean Witter.

Dean Witter's contract created no right for Dean Witter to stay plaintiffs' Virginia state law claims against Sears, and the Arbitration Act, however strongly favored, generously construed, or enthusiastically enforced, cannot itself create such a right. Section 3 delimits and codifies the federal policy favoring arbitration, and the district court either was required to issue a stay or it could issue no stay — it had no discretion, and the Second Circuit had no discretion. The Second Circuit's opinion directly conflicts with this Court's reasoning and comments in *Volt*, 109 S. Ct. at 1254 n. 5, and the Arbitration Act cannot be used to compel the arbitration of related litigation, absent agreement of the parties. *See Moses H. Cone Memorial Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 19-20 (1983) ("The latter dispute [with a third-party defendant] cannot be sent to arbitration without the [third party's] consent, since there is no arbitration agreement between [the plaintiff] and the [third party]");

Scherk v. Alberto-Culver Co., 417 U.S. 506, 511 (1974); *United Steelworkers of America v. Warrior & Gulf Navigation Co.*, 363 U.S. 574, 582 (1960) ("For arbitration is a matter of contract and a party cannot be required to submit to arbitration any dispute which he has not agreed so to submit").

"[T]he purpose of Congress" in adopting the Arbitration Act simply "was to make arbitration agreements as enforceable as other contracts, but not more so." *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 404 n.12 (1967). The Arbitration Act does not mandate unagreed arbitration.

All the Second Circuit had before it was *Sears'* appeal from the denial of *Sears'* request for a statutory, mandatory stay of the claims asserted against *Sears* — nothing more. Neither Sears nor Dean Witter has any agreement in writing for the arbitration of plaintiffs' Virginia state law claims asserted against Sears. Without such an applicable, written agreement, the claims in this action against Sears cannot be stayed under 9 U.S.C. § 3 pending arbitration. *Volt*, 109 S. Ct. at 1254; *Moses H. Cone*, 460 U.S. at 19-20; *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 (1985).

We know of no authority empowering the Second Circuit peremptorily to "stop all proceedings" against Sears while declining to determine Sears' appeal — the only appeal before the court.

CONCLUSION

The Second Circuit's decision improvidently expands the reach of "pendent appellate jurisdiction". Such jurisdiction cannot be exercised by a court of appeals solely on its own motion and never applies to an otherwise appealable order. As suggested by Mr. Justice White, this Court now should consider the limits to an exercise of this jurisdiction in light of this Court's decision in *Abney*. *See San Filippo v. United States Trust Co. of N.Y.*, 470 U.S. 1035, 1036 (1985) (White, J., dissenting to denial of certiorari). Moreover, as intimated in *Torres*, a court of appeals has no jurisdiction over a nonappealing party in a civil action.

An exercise of "pendent appellate jurisdiction" should never attach to an interlocutory order appealable under 9 U.S.C. § 15(a)(1)(A). Any order denying a mandatory stay is made fully appealable and usually applies peculiarly to the moving party. Pendent jurisdiction is unnecessary for such an appealable order and should not be available as a springboard for a plenary review of actions affecting other parties. An exercise of pendent jurisdiction should never be permitted on an appeal under 9 U.S.C. § 15(a)(1)(A) when the only appealing party (Sears) has no arbitration agreement. The invitation to future abuse is too great.

Also, as suggested by this Court in *Southland* and *Volt*, section 3 of the Arbitration Act applies only when a suit has been brought in federal court "upon [an] issue referable to arbitration under an agreement in writing" between the parties, a precondition not satisfied here.

Finally, grant of a mandatory stay for unagreed arbitration is contrary to this Court's decisions in *Volt*, *Moses H. Cone*, and other cases cited therein.

For these reasons, we respectfully ask this Court to grant this petition for certiorari and allow a review of the May 25, 1990, decision of the United States Court of Appeals for the Second Circuit.

Respectfully Submitted,

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APPENDIX

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

Nos. 918, 1197—August Term, 1989

(Argued: February 26, 1990 Decided: May 25, 1990)
Amended: July 10, 1990

Docket Nos. 89-9089, 90-7135

HORACE D. MCCOWAN, JR.
and SARAH E. MCCOWAN,

Plaintiffs-Appellees,

—v.—

SEARS, ROEBUCK AND CO.,
and DEAN WITTER REYNOLDS, INC.

Defendants-Appellants.

Before:

OAKES, KEARSE and WALKER,
Circuit Judges.[1]

Appeal from orders of the United States District Court for the Southern District of New York (Carter,

1 Judge Kearse disqualified herself after oral argument.

Judge), denying defendants' motions for a stay of court proceedings pending arbitration.

Judgment reversed.

CHARLES W. LAUGHLIN, Richmond, VA (Thompson & McMullan, Richmond, VA; Harry H. Wise, New York, NY, of counsel), *for Plaintiffs-Appellees*.

ELIZABETH HOOP FAY, Philadelphia, PA (John Linsenmeyer, John F.X. Peloso, Morgan, Lewis & Bockius, New York, NY, of counsel), *for Defendants-Appellants*.

WALKER, *Circuit Judge*.

Dean Witter Reynolds Inc. ("Dean Witter") and Sears, Roebuck and Co. ("Sears") appeal from orders of the United States District Court for the Southern District of New York (Robert L. Carter, *Judge*) denying their separate motions for a stay of court proceedings pending arbitration pursuant to section 3 of the Federal Arbitration Act (the "Act"), 9 U.S.C. § 3. For the reasons set forth below, we reverse the order of the district court denying Dean Witter a stay.

BACKGROUND

Plaintiffs Horace D. McCowan, Jr. and Sarah E. McCowan filed two lawsuits in 1986 claiming damages

arising from Dean Witter's allegedly fraudulent conduct in managing their securities account. The agreement between plaintiffs and Dean Witter under which the account was managed contained an arbitration clause.

On October 21, 1986, plaintiffs filed a complaint in the Southern District of New York against Dean Witter seeking damages for alleged violations of the Racketeering Influenced and Corrupt Organization Act ("RICO"), 18 U.S.C. § 1961 *et seq.*; sections 12(2) and 17(a) of the Securities Act of 1933 (the "1933 Act"), 15 U.S.C. §§ 77*l*(2), 77q(a); and sections 10(b) and 15(c)(1) of the Securities Exchange Act of 1934 (the "1934 Act"), 15 U.S.C. §§ 78j(b), 78o(c)(1). ("*McCowan I*").

On December 31, 1986, plaintiffs filed a second complaint in the United States District Court for the Eastern District of Virginia against both Dean Witter and Sears predicated on the same transactions which form the basis of the federal claims against Dean Witter initially filed in the Southern District of New York, alleging "controlling person liability" against Sears pursuant to the Virginia Securities Act, Va. Code Ann. § 13.1-501 *et seq.* ("*McCowan II*"). Although both Dean Witter and Sears were named as defendants in *McCowan II*, the complaint sought damages solely against Sears.

In April, 1987, the Virginia district court ordered *McCowan II* transferred to the Southern District of New York and denied without prejudice motions by Dean Witter and Sears to dismiss and for a stay of court proceedings pending arbitration. In May, 1987, *McCowan I* and *McCowan II* were consolidated before Judge Carter in the Southern District of New York. Thereafter, the district court referred the RICO and 1934 Act claims to arbitration, ordered the 1933 Act claims to be repleaded

and, pending the repleading, deferred decision on the motion to dismiss the state law claims. *McCowan v. Dean Witter Reynolds, Inc.*, 682 F. Supp. 741 (S.D.N.Y. 1987). Accordingly, the plaintiffs amended their *McCowan I* complaint.

Thereafter, the district court dismissed the 1933 Act claims on the grounds that section 17(a) does not afford a private right of action and section 12(2) does not apply to post-distribution transactions. *McCowan v. Dean Witter Reynolds, Inc.*, 1989 U.S. Dist. LEXIS 3711 (April 12, 1989). This left before the district court only the Virginia state law claims as originally pleaded in *McCowan II*. Dean Witter and Sears subsequently moved to dismiss those claims on the grounds that: (i) as to Dean Witter, the McCowans sought no relief; (ii) as to Sears, the McCowans failed to state a claim under the Virginia Securities Act because Sears was not a "controlling person"; and (iii) as to both Sears and Dean Witter, the McCowans failed to plead fraud with particularity as required by Fed. R. Civ. P. 9(b). In the alternative, Dean Witter moved for a stay pending arbitration pursuant to section 3 of the Federal Arbitration Act. Sears also sought a discretionary stay of the claims asserted against it pending arbitration of the underlying claims against Dean Witter.

On October 5, 1989, the district court denied defendants' motion to dismiss the claims in *McCowan II*. The court held that the Virginia Securities Act afforded the plaintiffs a private right of action for fraudulent security sales under section 13.1-522(a)(2); that Sears was a controlling person within the meaning of section 13.1-522(b) and that plaintiffs' allegations on that score were sufficient to state a claim; and, finally, that these fraud alle-

gations were pleaded with sufficient particularity to withstand scrutiny under Fed. R. Civ. P. 9(b). The court also denied Dean Witter's motion to be dismissed on the ground that no relief was sought from it. The court held that Dean Witter was an indispensable party to the action pursuant to Fed. R. Civ. P. 19 as liability existed for Sears only if the plaintiffs could demonstrate that Dean Witter violated the Virginia Act. Significant to this appeal, the court also denied the defendants' requests for a stay pending arbitration and directed them to answer the complaint.

On October 16, 1989, Sears and Dean Witter filed a Motion for Reargument and Clarification "pursuant to Local Rule 3(j) of the Civil Rules of the United States District Courts for the Southern and Eastern Districts of New York" on the grounds that the October 5, 1989 order "overlooks Dean Witter's right pursuant to the Federal Arbitration Act § 3 to have all controversies among Dean Witter Reynolds and the plaintiffs herein arbitrated and proceedings before this court stayed." The defendants sought an order granting Dean Witter a stay under section 3 of the Act and granting Sears a discretionary stay.

On November 6, 1989, Dean Witter learned from the judge's chambers that an order would be filed denying defendants' motion to reargue. That same day, after learning of the disposition of the reargument motion, Dean Witter, acting pursuant to Federal Arbitration Act section 15(a)(1)(A),[2] filed its Notice of Appeal from the

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2 9 U.S.C. § 15(a)(1)(A) provides that:

(a) An appeal may be taken from—

(1) an order—

(A) refusing a stay of any action under section 3 of this title.

district court's October 5, 1989 order. On November 8, 1989, the district court filed and the clerk entered an order, captioned "Endorsement," denying Dean Witter's motion for reargument. On November 17, 1989, Sears—having previously moved only for a discretionary stay—moved for a mandatory stay of the *McCowan II* claims against it pursuant to Federal Arbitration Act section 3. The district court denied Sears' motion on January 17, 1990. Sears appealed from this decision and we ordered consolidation of both appeals.

DISCUSSION

1. *Jurisdiction*

At the outset, we must address plaintiffs' argument that Dean Witter's appeal must be dismissed pursuant to Rule 4(a)(4) of the Federal Rules of Appellate Procedure on the ground that its notice of appeal, filed on November 6, 1989, was a nullity since it was filed while a Fed. R. Civ. P. 59(e) motion to alter or amend the judgment was pending. F.R.A.P. 4(a) states in pertinent part:

* * *

> (2) Except as provided in (a)(4) of this Rule 4, a notice of appeal filed after the announcement of a decision or order but before the entry of the judgment or order shall be treated as filed after such entry and on the day thereof.
>
> * * *
>
> (4) If a timely motion under the Federal Rules of Civil Procedure is filed in the district court by any party: (i) for judgment under Rule 50(b); (ii) under Rule 52(b) to amend or make additional findings of

> fact, whether or not an alteration of the judgment would be required if the motion is granted; (iii) under Rule 59 to alter or amend the judgment; or (iv) under Rule 59 for a new trial, the time for appeal for all parties shall run from the entry of the order denying a new trial or granting or denying any other such motion. *A notice of appeal filed before the disposition of any of the above motions shall have no effect.* A new notice of appeal must be filed within the prescribed time measured from the entry of the order disposing of the motion as provided above. No additional fees shall be required for such filing.

(emphasis added).

Plaintiffs argue that the district court's October 5, 1989 order was a judgment as defined by Fed. R. Civ. P. 54(a), that when Dean Witter filed its October 16 motion to reargue, it was a timely motion "under Rule 59 to alter or amend the judgment," and, since Dean Witter's November 6 Notice of Appeal was filed "before the disposition" of that motion, it had "no effect." Plaintiffs maintain that because Dean Witter never filed a timely notice of appeal after the order denying the motion for reargument was entered on November 8, we are without jurisdiction to hear the appeal.

Dean Witter responds with a welter of arguments designed to extricate itself from this apparent predicament. First it contends that the motion for reargument was not made pursuant to Rule 59(e) but pursuant to Rule 3(j) of the Local Rules of the Southern and Eastern Districts of New York. Next it argues that the October 5 order from which it appealed was not a

"judgment" within the meaning of Rule 59(e) because it was interlocutory, it did not involve a reconsideration of the merits and no separate document was filed pursuant to Rule 58. Finally, Dean Witter argues that the Notice of Appeal should be treated as if filed after the district court's disposition of its post-decisional motion.

F.R.A.P. 4(a)(4) is jurisdictional and unequivocal. *Spika v. Village of Lombard*, 763 F.2d 282, 284 (7th Cir. 1985), *cert. denied*, 474 U.S. 1056 (1986). A notice of appeal filed by any party while a timely post-decisional motion specified in the rule is *sub judice* is a nullity. "[I]t is as if no notice of appeal were filed at all . . . [and] the Court of Appeals lacks jurisdiction to act." *Griggs v. Provident Consumer Discount Co.*, 459 U.S. 56, 61 (1982). Appeals from final judgments have regularly been dismissed for want of jurisdiction after notices of appeal have been obliterated by the rule. *See, e.g., Fisher v. Klein*, 873 F.2d 626, 627 (2d Cir. 1989); *Rados v. Celotex*, 809 F.2d 170, 172 (2d Cir. 1986); Wright, Miller, Cooper and Gressman, *Federal Practice and Procedure*, Jurisdiction § 3950 at 361 (1977 and Supp. 1990). Judge Posner has appropriately termed Rule 4(a) a "trap for the unwary into which many appellants, especially those not represented by counsel . . . have fallen, with dire consequences since there is no way they can reinstate their appeal if the second notice of appeal is untimely." *Averhart v. Arrendondo*, 773 F.2d 919, 920 (7th Cir. 1985).

Rule 4(a)(4) is a trap not because it is unclear, but because it is buried in Rule 4 of the Rules of Appellate Procedure with which most litigants have less familiarity than they do with the Federal Rules of Civil Procedure. Moreover, as Judge Posner stated in *Averhart*,

> [t]he idea that the first notice of appeal lapses [or is a nullity if filed while the post-decisional motion is pending] rather than merely being suspended is not intuitive, so unless a litigant has a pretty good understanding of how Rule 59 of the [civil] procedure rules interacts with Rule 4 of the appellate rules, he is apt to fall into the same hole into which Mr. Averhart has disappeared.

Averhart, 773 F.2d at 920.

Rule 4 makes the post-decisional and appeals process more efficient in several ways. By invalidating a notice of appeal filed while a motion to reargue is pending in the district court, the rule prevents duplicative substantive review in two different courts. By ensuring that the district judge pass first on disputed issues, the rule also helps narrow relevant issues for appeal and avoids unnecessary remands. And, finally, the rule affords an appellate court the opportunity to consider the district judge's assessment of the issues ultimately raised on appeal. *See Griggs*, 459 U.S. at 60 n.2 (citing Notes of Advisory Committee on Appellate Rules, 28 U.S.C. App., p. 146 (1976 ed., Supp. V)).

Most of Dean Witter's arguments are premised on the fact that the order appealed from was not a final judgment disposing of the litigation. But neither Rule 4(a)(4) nor Rule 59(e) are confined to final judgments. They apply to any "judgment," defined in Fed. R. Civ. P. 54(a) to include "a decree and any order from which an appeal lies." Such an order includes an interlocutory order like the one at issue here, made appealable by statute. *See* 6 Moore's *Federal Practice* ¶ 54.02 at 54-23 (2d ed. 1988). The October 5 order is no less a judgment because no "separate document" was filed pursuant to

Fed. R. Civ. P. 58. We assume, without deciding, that the requirements for an effective judgment set forth in Rule 58 must generally be satisfied before this court's jurisdiction may be invoked pursuant to 9 U.S.C. § 15(a)(1)(A). However, Dean Witter waived the "separate document" requirement when it sought to appeal by filing its now challenged notice on November 6 in the absence of such a document. *See Bankers Trust Co. v. Mallis*, 435 U.S. 381, 388 (1978).

Although Dean Witter labeled its motion to reargue as one under Rule 3(j) of the local rules, most substantive motions brought within ten days of the entry of judgment are functionally motions under Rule 59(e), regardless of their label or whether relief might also have been obtained under another provision. *Lyell Theatre Corp. v. Loews Corp.*, 682 F.2d 37, 40-41 (2d Cir. 1982); 9 Moore's *Federal Practice* § 204.12[1] at 4-73 (2d ed. 1990); *see also* 6A Moore's *Federal Practice* § 59.12 (1) at 59-265-66 (2d ed. 1989). We reject Dean Witter's assertion that its motion to reargue the stay application is not a substantive motion to reargue the merits and thus is not a Rule 59(e) motion. The motion was one to reargue the merits of the question forming the basis of the appeal—namely, the denial of the stay—and thus was properly one under Rule 59(e). The fact that the order appealed from is interlocutory does not change the interplay between Rule 59(e) and Rule 4(a)(4); the interest in harmonizing the operations of the district and appellate courts where post-decisional review is sought remains the same whether the district court decision appealed from is interlocutory or a final judgment.

Finally, Dean Witter's notice of appeal filed on November 6, two days before the entry of the district court's order denying the motion to reargue, is not saved by F.R.A.P. 4 (a)(2). In a decision that neither party brought to our attention, the Supreme Court explained the interplay between Rules 4(a)2 and (a)(4).

> Rule 4(a)4 specifically states that a notice of appeal, to be effective, must be "filed within the prescribed time measured from entry of the order disposing of the motion as provided above." Rule 4(a)(2) provides that "*[e]xcept as provided in (a)(4) of this Rule 4*, a notice of appeal filed after the announcement of a decision or order but before the entry of the judgment or order shall be treated as filed after such entry and on the day thereof" (emphasis added). The plain import of this language is that with respect to the particular motions to which it applies, Rule 4(a)(4) constitutes an exception to the general rule that a notice of appeal filed after announcement of an order but before its entry in the docket will be deemed timely filed.

Acosta v. Louisiana Department of Health and Human Resources, 478 U.S. 251, 253-4 (1986). "Any other interpretation," the Court explained, "would read the first clause of subdivision (a)(2) out of Rule 4 by holding that Rule 4(a)(4) does *not* constitute such an exception." Thus, the Supreme Court strictly construed the language of Rule 4(a)(4) and found ineffectual a notice of appeal filed after the oral announcement of a denial of a Rule 59 motion and before the entry of the written order memorializing the denial. Accordingly, the November 6 notice of appeal is not preserved by Rule 4(a)(2). Plaintiffs argue that because Dean Witter did

not file a new notice following the entry of the order denying the motion for reargument, we are without jurisdiction to hear its appeal. We disagree.

Although Dean Witter's notice of appeal does not accord us jurisdiction of the district court's denial of its request for a mandatory stay, we may exercise pendent jurisdiction based on the timely appeal by Sears from the district court's ruling on Sears' motion for a stay pursuant to section 3 of the Federal Arbitration Act. Where the court has unquestioned jurisdiction of a cause "it would be absurd to require the court to close its eyes to another interlocutory order which, though not itself appealable, might infect the entire proceeding with error and thus require reversal after large expenditure of judicial and professional time." *Semmes Motors, Inc. v. Ford Motor Company*, 429 F.2d 1197, 1201 (2d Cir. 1970) (Friendly, J.).

The guiding principle informing the discretionary application of pendent jurisdiction is whether review of the appealable order will involve consideration of factors relevant to the otherwise nonappealable order. *See General Motors Corporation v. City of New York*, 501 F.2d 639, 648 (2d Cir. 1974); *see also San Filippo v. U.S. Trust Co. of New York, Inc.*, 737 F.2d 246, 255 (2d Cir. 1984), *cert. denied*, 470 U.S. 1035 (1985) (court may consider nonappealable issues where there is "sufficient overlap" in the factors relevant to the appealable and nonappealable issues in the case). While this doctrine has been utilized more commonly by this court to take jurisdiction over issues pendent to those before it—the parties being the same, it may also be invoked to entertain appeals by parties not otherwise entitled to appeal on a theory of pendent party jurisdiction. *See*,

e.g., *U.S. v. Tom*, 787 F.2d 65, 68 n.3. (2d Cir. 1986); *Barrett v. United States*, 798 F.2d 565, 570-71 (2d Cir. 1986).

We are mindful that "pendent appellate jurisdiction is a procedural device that should rarely be used because of the danger of abuse." *Akerman v. Oryx Communications, Inc.*, 810 F.2d 336, 339 (2d Cir. 1987) (citing *Marcera v. Chinlund*, 595 F.2d 1231, 1245 (2d Cir. 1977) (Van Graafeiland, J., dissenting) *vacated on other grounds sub nom. Lombard v. Marcera*, 442 U.S. 915 (1979)). While we do not believe that litigants should generally be permitted to circumvent the rules of appellate procedure by obtaining review of otherwise nonappealable orders on the coattails of an appealable order, under the circumstances of this case, we find the exercise of pendent appellate jurisdiction warranted. The issues in Sears' and Dean Witter's appeals overlap substantially. Each appeal requires analysis of the arbitration agreement entered into by the plaintiffs and Dean Witter. Furthermore, determination of the appropriateness of a stay for either party requires examination of the relationship between the defendants and the basis upon which the plaintiffs assert liability against them. Under these circumstances, and in view of the fact that but for Dean Witter's inadvertent procedural default this Court would have had jurisdiction over Dean Witter's fully briefed and argued appeal, pendent review of the district court's denial of Dean Witter's stay is a wise and time-saving exercise of our discretion. We thus turn to the merits.

2. *The Denial of Stays Pending Arbitration*

Both Dean Witter and Sears argue that the district court erred in not granting their requests for stays pend-

ing arbitration of the Virginia Securities Act claims asserted in *McCowan II*. In its October 5 order, the district court, apparently treating its power to grant a stay as to both defendants as discretionary pursuant to *Moses H. Cone Memorial Hosp. v. Mercury Construction Corp.*, 460 U.S. 1, 20 n.23 (1983), denied both requests. As we have noted, Dean Witter then filed a motion to reargue in which it reasserted that it had a right to a stay pursuant to section 3 of the Federal Arbitration Act. The district court's "Endorsement" filed November 8, "affirm[ed] its earlier ruling denying the defendants' motion for a stay pending the outcome of arbitration." The court found that Dean Witter was a "primary actor" and was, therefore, properly joined as an indispensable party. While not referring to section 3 of the Act or discussing its reach, the district court stated:

> The court recognizes that Dean Witter has an arbitration agreement with the plaintiffs. However, the dispute in this case is between the plaintiffs and Sears, and no judgment is, or can be, demanded of Dean Witter. The plaintiffs have made allegations against Sears which are properly adjudicated in this forum, and they are entitled to timely consideration of their claims.

On November 17, 1989, Sears, which had previously requested only a discretionary stay pending arbitration of the claims against Dean Witter, moved pursuant to section 3 of the Arbitration Act for a mandatory stay and referral of the claims against it to arbitration. On January 17, 1990, the court denied Sears' motion finding that Sears was neither a party to an arbitration agreement with plaintiffs nor an intended beneficiary of

the agreement between Dean Witter and the McCowans. The district court stated that "[a]lthough Sears may be an incidental beneficiary of the arbitration agreement, clearly the plaintiffs and Dean Witter did not make this contract to confer a direct benefit on Sears."

Before we turn to the Federal Arbitration Act, it is important to examine briefly the nature of the claims asserted in *McCowan II*. Plaintiffs allege that Dean Witter conducted fraudulent unauthorized trades in the account it managed for them in violation of the Virginia Securities Act § 13.1-522(a). Their claim against Sears is based solely on Sears' status as a controlling person of Dean Witter. Virginia Securities Act § 13.1-522.C. Plaintiffs attribute no fraudulent conduct to Sears and, all agree, no recovery against Sears is possible unless plaintiffs first prove their claim against Dean Witter.

In enacting the Federal Arbitration Act, Congress created national substantive law governing all questions of the validity and enforceability of arbitration agreements within its scope. *Genesco, Inc. v. T. Kakiuchi & Co., Ltd.*, 815 F.2d 840, 845 (2d Cir. 1987) (citing *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 626 (1985)); *see also Moses H. Cone*, 460 U.S. at 24; *Varley v. Tarrytown Associates, Inc.*, 477 F.2d 208, 209 (2d Cir. 1973). Hence, whether plaintiffs are bound by the arbitration clause of the contract with Dean Witter is a matter of federal law, which incorporates generally accepted principles of contract law. *See Genesco*, 815 F.2d at 845 (citing *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 404-05 (1967)). Accordingly, section 2 of the Act provides that arbitration provisions "shall be valid, irrevocable and enforceable, save upon such grounds as exist at law or

in equity for the revocation of any contract." 9 U.S.C. § 2.

Section 3 of the Act provides:

> § 3. Stay of proceedings where issue therein referable to arbitration
>
> If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration.

A commonsense reading of this section suggests that if there is a federal action "upon" an "issue referable to arbitration" by the terms of an arbitration agreement, then the federal court must "stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement."

The relevant arbitration clause agreed to by plaintiffs and Dean Witter states that "any controversy between [Dean Witter] and the undersigned [plaintiffs] arising out of or relating to this contract or the breach thereof shall be settled by arbitration." Plaintiffs do not claim that the dispute in *McCowan II*, does not "aris[e] out of" or "relat[e] to" the contract containing the arbitration clause, nor could they. Indeed, it is Dean Witter's alleged mishandling of the very account opened in con-

nection with the parties' contract that is at issue in both *McCowan I* and *McCowan II*. The district court determined as much when it granted the stay in *McCowan I* of federal claims based on the same allegations of misconduct—a decision which was clearly correct in light of *Shearson American Express v. McMahon*, 482 U.S. 220 (1987). Rather, plaintiffs assert that there exists no arbitrable "controversy" between them and Dean Witter in *McCowan II* because no judgment is sought against Dean Witter in that action.

We believe that the absence of a request for relief against Dean Witter does not determine whether a controversy exists between Dean Witter and plaintiffs, and that the district court erred when it held that the absence of a request for a judgment against Dean Witter, barred Dean Witter from invoking the agreement. Although fashioned as two separate lawsuits, there is in reality a single "controversy" at issue—as that term would have been understood by the contracting parties—giving rise to claims under three separate laws: the 1934 Act, RICO and the Virginia Securities Act. The first two demand a money judgment from Dean Witter; the third requires a showing of liability against Dean Witter as a predicate to recovery against Sears, but demands no monetary judgment from Dean Witter. Dean Witter's contractual right to arbitrate "any controversy" arising out of or relating to the contract between the parties would be seriously impaired if *McCowan II* were not stayed pending arbitration. Under these circumstances, we believe that Dean Witter has a right to the mandatory stay afforded by section 3 of the Act.

Dean Witter is involved in a "controversy," as that term is commonly understood, with plaintiffs over its

management of their account. *See* Webster's Third New International Dictionary 497 (1981) ("the act of disputing or contending . . . a cause, occasion, or instance of disagreement or contention"). Even if the parties intended to arbitrate controversies defined as "a suit in law or equity," *McCowan II* is such a suit, *see* Black's Law Dictionary 298 (4th ed. 1979), and Dean Witter as a named defendant would be obliged, if the suit were to proceed, to file an answer and bear the costs of its defense.

Moreover, the presence of the *McCowan I* federal claims before the arbitrator weighs heavily in favor of a stay of the state law claims in *McCowan II*. If *McCowan II* were allowed to proceed against Dean Witter in federal court, Dean Witter's right to arbitrate the federal claims already referred to arbitration in *McCowan I* would be impaired since any issues determined against Dean Witter in court proceedings in *McCowan II* could have collateral estoppel effect on the arbitration. *See Dickson v. Heinold Securities, Inc.*, 661 F.2d 638, 644 (7th Cir. 1981); *Mansbach v. Prescott, Ball, Turben*, 598 F.2d 1017, 1031 (6th Cir. 1979) (principles of collateral estoppel prevent relitigation of issues in arbitration that have already been decided in federal court); *N.Y.S. Ass'n for Retarded Children v. Carey*, 456 F. Supp. 85, 96 (E.D.N.Y. 1978), *aff'd* 596 F.2d 27 (2d Cir. 1979); *J.D. Marshall Intern, Inc. v. Redstart, Inc.*, 656 F. Supp. 830, 834 (N.D. Ill. 1987) (prior federal proceeding has full collateral estoppel and res judicata effects on subsequent arbitration). While section 13.1-522(a) of the Virginia Securities Act differs from Rule 10b-5 of the 1934 Act by placing the burden of disproving scienter on the defendant rather than requiring the plaintiff to prove it, and by making negligent as well

as intentional misrepresentations actionable, *see* 4 A. Bromberg & L. Lowenfels, *Securities Fraud & Commodities Fraud*, § 8.4, pp. 204.1, 204.146, 204.170 (1989), in other respects certain elements of the state and federal offenses appear to be the same, including a failure to disclose, materiality and causation. *Id.* at § 8.1, p. 195. According to Professor Loss, the Virginia statute, like other state fraud statutes modeled after section 101 of the Uniform Securities Act, "is substantially the SEC's rule 10b-5." *See* L. Loss, *Commentary on the Uniform Securities Act*, 6 (1976). Thus, the preclusive effect of court action in *McCowan II* in the *McCowan I* arbitration is potentially substantial and significant.

Our interpretation of the arbitration agreement to include the *McCowan II* claims against Dean Witter furthers and is supported by the "liberal federal policy favoring arbitration." *Moses H. Cone*, 460 U.S. at 24. "The legislative history of the Act establishes that the purpose behind its passage was to ensure judicial enforcement of privately made agreements to arbitrate." *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213, 219 (1985); *see also Mitsubishi Motors Corp.*, 473 U.S. at 625. Thus, we conclude that the *McCowan II* claims against Dean Witter must be stayed pending arbitration under section 3 of the Arbitration Act.

Sears moved in the district court for a stay of *McCowan II* as an exercise of the district court's discretion at the same time Dean Witter moved pursuant to Arbitration Act section 3. After the district court denied both motions, Sears moved for a section 3 stay claiming a right to enforce the arbitration agreement as a third party beneficiary of the agreement or based on its status as a "controlling person" of Dean Witter. In view of

our holding that Dean Witter is entitled to a mandatory section 3 stay, we need not determine whether Sears also has such a right. The practical effect of the stay as to Dean Witter, an indispensable party in *McCowan II*, is that the suit against Sears, which is wholly dependent on the claim against Dean Witter, cannot proceed.

Judgment reversed.

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

Nos. 918, 1197—August Term 1989

(Argued: February 26, 1990 Decided: May 25, 1990)

Docket Nos. 89-9089, 90-7135

HORACE D. MCCOWAN, JR. and
SARAH E. MCCOWAN,

Plaintiffs-Appellees,

—v.—

SEARS, ROEBUCK AND CO., and
DEAN WITTER REYNOLDS, INC.,

Defendants-Appellants.

Before:

OAKES, KEARSE and WALKER,

Circuit Judges.[1]

Appeal from orders of the United States District Court for the Southern District of New York (Carter,

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[1] Judge Kearse disqualified herself after oral argument.

Judge), denying defendants' motions for a stay of court proceedings pending arbitration.

Judgment reversed.

CHARLES W. LAUGHLIN, Richmond, VA (Thompson & McMullan, Richmond, VA; Harry H. Wise, New York, NY, of counsel), *for Plaintiffs-Appellees*.

ELIZABETH HOOP FAY, Philadelphia, PA (John Linsenmeyer, John V.X. Peloso, Morgan, Lewis & Bockius, New York, NY, of counsel), *for Defendants-Appellants*.

WALKER, *Circuit Judge*:

Dean Witter Reynolds Inc. ("Dean Witter") and Sears, Roebuck and Co. ("Sears") appeal from orders of the United States District Court for the Southern District of New York (Robert L. Carter, *Judge*) denying their separate motions for a stay of court proceedings pending arbitration pursuant to section 3 of the Federal Arbitration Act (the "Act"), 9 U.S.C. § 3. We reverse the judgments of the district court.

BACKGROUND

Plaintiffs Horace D. McCowan, Jr. and Sarah E. McCowan filed two lawsuits in 1986 claiming damages arising from Dean Witter's allegedly fraudulent conduct

in managing their securities account. The agreement between plaintiffs and Dean Witter under which the account was managed contained an arbitration clause.

On October 21, 1986, plaintiffs filed a complaint in the Southern District of New York against Dean Witter seeking damages for alleged violations of the Racketeering Influenced and Corrupt Organization Act ("RICO"), 18 U.S.C. § 1961 *et seq.*; sections 12(2) and 17(a) of the Securities Act of 1933 (the "1933 Act"), 15 U.S.C. §§ 77*l*(2), 77q(a); and sections 10(b) and 15(c)(1) of the Securities Exchange Act of 1934 (the "1934 Act"), 15 U.S.C. §§ 78j(b), 78o(c)(1). ("*McCowan I*").

On December 31, 1986, plaintiffs filed a second complaint in the United States District Court for the Eastern District of Virginia against both Dean Witter and Sears predicated on the same transactions which form the basis of the federal claims against Dean Witter initially filed in the Southern District of New York, alleging "controlling person liability" against Sears pursuant to the Virginia Securities Act, Va. Code Ann. § 13.1-501 *et seq.* ("*McCowan II*"). Although both Dean Witter and Sears were named as defendants in *McCowan II*, the complaint sought damages solely against Sears.

In April, 1987, the Virginia district court ordered *McCowan II* transferred to the Southern District of New York and denied without prejudice motions by Dean Witter and Sears to dismiss and for a stay of court proceedings pending arbitration. In May, 1987, *McCowan I* and *McCowan II* were consolidated before Judge Carter in the Southern District of New York. Thereafter, the district court referred the RICO and 1934 Act claims to arbitration, ordered the 1933 Act claims to be repleaded and, pending the repleading, deferred decision on the

motion to dismiss the state law claims. *McCowan v. Dean Witter Reynolds, Inc.*, 682 F. Supp. 741 (S.D.N.Y. 1987). Accordingly, the plaintiffs amended their *McCowan I* complaint.

Thereafter, the district court dismissed the 1933 Act claims on the grounds that section 17(a) does not afford a private right of action and section 12(2) does not apply to post-distribution transactions. *McCowan v. Dean Witter Reynolds, Inc.*, 1989 U.S. Dist. LEXIS 3711 (April 12, 1989). This left before the district court only the Virginia state law claims as originally pleaded in *McCowan II*. Dean Witter and Sears subsequently moved to dismiss those claims on the grounds that: (i) as to Dean Witter, the McCowans sought no relief; (ii) as to Sears, the McCowans failed to state a claim under the Virginia Securities Act because Sears was not a "controlling person"; and (iii) as to both Sears and Dean Witter, the McCowans failed to plead fraud with particularity as required by Fed. R. Civ. P. 9(b). In the alternative, Dean Witter moved for a stay pending arbitration pursuant to section 3 of the Federal Arbitration Act. Sears also sought a discretionary stay of the claims asserted against it pending arbitration of the underlying claims against Dean Witter.

On October 5, 1989, the district court denied defendants' motion to dismiss the claims in *McCowan II*. The court held that the Virginia Securities Act afforded the plaintiffs a private right of action for fraudulent security sales under section 13.1-522(a)(2); that Sears was a controlling person within the meaning of section 13.1-522(b) and that plaintiffs' allegations on that score were sufficient to state a claim; and, finally, that these fraud allegations were pleaded with sufficient particularity to

withstand scrutiny under Fed. R. Civ. P. 9(b). The court also denied Dean Witter's motion to be dismissed on the ground that no relief was sought from it. The court held that Dean Witter was an indispensable party to the action pursuant to Fed. R. Civ. P. 19 as liability existed for Sears only if the plaintiffs could demonstrate that Dean Witter violated the Virginia Act. Significant to this appeal, the court also denied the defendants' requests for a stay pending arbitration and directed them to answer the complaint.

On October 16, 1989, Sears and Dean Witter filed a Motion for Reargument and Clarification "pursuant to Local Rule 3(j) of the Civil Rules of the United States District Courts for the Southern and Eastern Districts of New York" on the grounds that the October 5, 1989 order "overlooks Dean Witter's right pursuant to the Federal Arbitration Act § 3 to have all controversies among Dean Witter Reynolds and the plaintiffs herein arbitrated and proceedings before this court stayed." The defendants sought an order granting Dean Witter a stay under section 3 of the Act and granting Sears a discretionary stay.

On November 6, 1989, Dean Witter learned from the judge's chambers that an order would be filed denying defendants' motion to reargue. That same day, after learning of the disposition of the reargument motion, Dean Witter, acting pursuant to Federal Arbitration Act section 15(a)(1)(A),[2] filed its Notice of Appeal from the district court's October 5, 1989 order. On November 8,

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2 9 U.S.C. § 15(a)(1)(A) provides that:

(a) An appeal may be taken from—

(1) an order—

(A) refusing a stay of any action under section 3 of this title.

1989, the district court filed and the clerk entered an order, captioned "Endorsement," denying Dean Witter's motion for reargument. On November 17, 1989, Sears—having previously moved only for a discretionary stay—moved for a mandatory stay of the *McCowan II* claims against it pursuant to Federal Arbitration Act section 3. The district court denied Sears' motion on January 17, 1990. Sears appealed from this decision and we ordered consolidation of both appeals.

DISCUSSION

1. *Appellate Jurisdiction*

At the outset, we must address plaintiffs' argument that Dean Witter's appeal must be dismissed pursuant to Rule 4(a)(4) of the Federal Rules of Appellate Procedure on the ground that its notice of appeal, filed on November 6, 1989, was a nullity since it was filed while a Fed. R. Civ. P. 59(e) motion to alter or amend the judgment was pending. F.R.A.P. 4(a) states in pertinent part:

* * *

> (2) Except as provided in (a)(4) of this Rule 4, a notice of appeal filed after the announcement of a decision or order but before the entry of the judgment or order shall be treated as filed after such entry and on the day thereof.
>
> * * *
>
> (4) If a timely motion under the Federal Rules of Civil Procedure is filed in the district court by any party: (i) for judgment under Rule 50(b); (ii) under Rule 52(b) to amend or make additional findings of fact, whether or not an alteration of the judgment would be required if the motion is granted; (iii)

> under Rule 59 to alter or amend the judgment; or (iv) under Rule 59 for a new trial, the time for appeal for all parties shall run from the entry of the order denying a new trial or granting or denying any other such motion. *A notice of appeal filed before the disposition of any of the above motions shall have no effect.* A new notice of appeal must be filed within the prescribed time measured from the entry of the order disposing of the motion as provided above. No additional fees shall be required for such filing.

(emphasis added).

Plaintiffs argue that the district court's October 5, 1989 order was a judgment as defined by Fed. R. Civ. P. 54(a), that when Dean Witter filed its October 16 motion to reargue, it was a timely motion "under Rule 59 to alter or amend the judgment," and, since Dean Witter's November 6 Notice of Appeal was filed "before the disposition" of that motion, it had "no effect." Plaintiffs maintain that because Dean Witter never filed a timely notice of appeal after the order denying the motion for reargument was entered on November 8, we are without jurisdiction to hear the appeal.

Dean Witter responds with a welter of arguments designed to extricate itself from this apparent predicament. First it contends that the motion for reargument was not made pursuant to Rule 59(e) but pursuant to Rule 3(j) of the Local Rules of the Southern and Eastern Districts of New York. Next it argues that the October 5 order from which it appealed was not a "judgment" within the meaning of Rule 59(e) because it was interlocutory, it did not involve a reconsideration of

the merits and no separate document was filed pursuant to Rule 58. Finally, Dean Witter argues that the Notice of Appeal should be treated as if filed after the district court's disposition of its post-decisional motion.

F.R.A.P. 4(a)(4) is jurisdictional and unequivocal. *Spika v. Village of Lombard*, 763 F.2d 282, 284 (7th Cir. 1985), *cert. denied*, 474 U.S. 1056 (1986). A notice of appeal filed by any party while a timely post-decisional motion specified in the rule is *sub judice* is a nullity. "[I]t is as if no notice of appeal were filed at all . . . [and] the Court of Appeals lacks jurisdiction to act." *Griggs v. Provident Consumer Discount Co.*, 459 U.S. 56, 61 (1982). Appeals from final judgments have regularly been dismissed for want of jurisdiction after notices of appeal have been obliterated by the rule. *See, e.g., Fisher v. Klein*, 873 F.2d 626, 627 (2d Cir. 1989); *Rados v. Celotex*, 809 F.2d 170, 172 (2d Cir. 1986); Wright, Miller, Cooper and Gressman, *Federal Practice and Procedure*, Jurisdiction § 3950 at 361 (1977 and Supp. 1990). Judge Posner has appropriately termed Rule 4(a) a "trap for the unwary into which many appellants, especially those not represented by counsel . . . have fallen, with dire consequences since there is no way they can reinstate their appeal if the second notice of appeal is untimely." *Averhart v. Arrendondo*, 773 F.2d 919, 920 (7th Cir. 1985).

Rule 4(a)(4) is a trap not because it is unclear, but because it is buried in Rule 4 of the Rules of Appellate Procedure with which most litigants have less familiarity than they do with the Federal Rules of Civil Procedure. Moreover, as Judge Posner stated in *Averhart*,

> [t]he idea that the first notice of appeal lapses [or is a nullity if filed while the post-decisional motion is

> pending] rather than merely being suspended is not intuitive, so unless a litigant has a pretty good understanding of how Rule 59 of the [civil] procedure rules interacts with Rule 4 of the appellate rules, he is apt to fall into the same hole into which Mr. Averhart has disappeared.

Averhart, 773 F.2d at 920.

Rule 4 makes the post-decisional and appeals process more efficient in several ways. By invalidating a notice of appeal filed while a motion to reargue is pending in the district court, the rule prevents duplicative substantive review in two different courts. By ensuring that the district judge pass first on disputed issues, the rule also helps narrow relevant issues for appeal and avoids unnecessary remands. And, finally, the rule affords an appellate court the opportunity to consider the district judge's assessment of the issues ultimately raised on appeal. *See Griggs*, 459 U.S. at 60 n.2 (citing Notes of Advisory Committee on Appellate Rules, 28 U.S.C. App., p. 146 (1976 ed., Supp. V)).

Most of Dean Witter's arguments are premised on the fact that the order appealed from was not a final judgment disposing of the litigation. But neither Rule 4(a)(4) nor Rule 59(e) are confined to final judgments. They apply to any "judgment," defined in Fed. R. Civ. P. 54(a) to include "a decree and any order from which an appeal lies." Such an order includes an interlocutory order like the one at issue here, made appealable by statute. *See* 6 Moore's *Federal Practice* ¶ 54.02 at 54-23 (2d ed. 1988). The October 5, order is no less a judgment because no "separate document" was filed pursuant to Fed. R. Civ. P. 58. We assume, without deciding, that the requirements for an effective judgment set forth

in Rule 58 must generally be satisfied before this court's jurisdiction may be invoked pursuant to 9 U.S.C. § 15(a)(1)(A). However, Dean Witter waived the "separate document" requirement when it sought to appeal by filing its now challenged notice on November 6 in the absence of such a document. *See Bankers Trust Co. v. Mallis*, 435 U.S. 381, 388 (1978).

Although Dean Witter labeled its motion to reargue as one under Rule 3(j) of the local rules, most substantive motions brought within ten days of the entry of judgment are functionally motions under Rule 59(e), regardless of their label or whether relief might also have been obtained under another provision. *Lyell Theatre Corp. v. Loews Corp.*, 682 F.2d 37, 40-41 (2d Cir. 1982); 9 Moore's *Federal Practice* § 204.12[1] at 4-73 (2d ed. 1990); *see also* 6A Moore's *Federal Practice* § 59.12(1) at 59-265-66 (2d ed. 1989). We reject Dean Witter's assertion that its motion to reargue the stay application is not a substantive motion to reargue the merits and thus is not a Rule 59(e) motion. The motion was one to reargue the merits of the question forming the basis of the appeal—namely, the denial of the stay—and thus was properly one under Rule 59(e). The fact that the order appealed from is interlocutory does not change the interplay between Rule 59(e) and Rule 4(a)(4); the interest in harmonizing the operations of the district and appellate courts where post-decisional review is sought remains the same whether the district court decision appealed from is interlocutory or a final judgment.

Nonetheless, we believe that we have jurisdiction because Rule 4(a)(2) requires us to treat Dean Witter's November 6 notice as filed after the "disposition" of the Rule 59(e) motion notwithstanding that the "disposi-

tion" was not entered by the clerk until November 8. Rule 4(a)(2) provides that "a notice of appeal filed after the announcement of a decision or order but before the entry of the judgment or order shall be treated as filed after such entry and on the day thereof." To be sure, this language is preceded by the phrase "[e]xcept as provided in (a)(4) of this Rule 4"; however, as the Advisory Committee Note states, the exception is for "cases in which a post-trial motion has destroyed the finality of the judgment," which we take to refer to cases in which a post-decisional motion is filed before the entry of the order appealed from but after its announcement. Thus, we believe that the exception in Rule 4(a)(2) is designed to remove the conflict between Rule 4(a)(2) and Rule (a)(4) that would otherwise occur if, between announcement of an appealable order and its entry, both a post-decisional motion and notice of appeal were filed, and does not cover the situation where, as in this case, the announcement at issue is the disposition of the earlier filed post-decisional motion. Accordingly, we are free to apply Rule 4(a)(2) to this case.

Rule 4(a)(2) speaks of an "announcement" before entry and, while we question whether learning of the motion's disposition from the judge's chambers is an "announcement," we see no reason not to apply the rule in such a circumstance. In this case, the "announcement" of the court's disposition of the post-decisional motion effectively ensured that the goals of Rule 4(a)(4) were met. Since the district court had already ruled on the motion for reargument, the objective of prior district court review was achieved and the possibility of simultaneous, duplicative proceedings in different courts had thus been removed. Furthermore, the outcome of the post-decisional motion has been presented to us for

consideration and no prejudice has been shown. Pursuant to Rule 4(a)(2), then, the filing of the Notice of Appeal on November 6, 1989, after Dean Witter learned from chambers of the district court's disposition of the post-decisional motion is treated as filed after its entry on November 8, 1989. Accordingly, we have jurisdiction. We now turn to the merits of the appeals.

2. *The Denials of Stays Pending Arbitration*

Both Dean Witter and Sears argue that the district court erred in not granting their requests for stays pending arbitration of the Virginia Securities Act claims asserted in *McCowan II*. In its October 5 order, the district court, apparently treating its power to grant a stay as to both defendants as discretionary pursuant to *Moses H. Cone Memorial Hosp. v. Mercury Construction Corp.*, 460 U.S. 1, 20 n.23 (1983), denied both requests. As we have noted, Dean Witter then filed a motion to reargue in which it reasserted that it had a right to a stay pursuant to section 3 of the Federal Arbitration Act. The district court's "Endorsement" filed November 8, "affirm[ed] its earlier ruling denying the defendants' motion for a stay pending the outcome of arbitration." The court found that Dean Witter was a "primary actor" and was, therefore, properly joined as an indispensable party. While not referring to section 3 of the Act or discussing its reach, the district court stated:

> The court recognizes that Dean Witter has an arbitration agreement with the plaintiffs. However, the dispute in this case is between the plaintiffs and Sears, and no judgment is, or can be, demanded of Dean Witter. The plaintiffs have made allegations

> against Sears which are properly adjudicated in this forum, and they are entitled to timely consideration of their claims.

On November 17, 1989, Sears, which had previously requested only a discretionary stay pending arbitration of the claims against Dean Witter, moved pursuant to section 3 of the Arbitration Act for a mandatory stay and referral of the claims against it to arbitration. On January 17, 1990, the court denied Sears' motion finding that Sears was neither a party to an arbitration agreement with plaintiffs nor an intended beneficiary of the agreement between Dean Witter and the McCowans. The district court stated that "[a]lthough Sears may be an incidental beneficiary of the arbitration agreement, clearly the plaintiffs and Dean Witter did not make this contract to confer a direct benefit on Sears."

Before we turn to the Federal Arbitration Act, it is important to examine briefly the nature of the claims asserted in *McCowan II*. Plaintiffs allege that Dean Witter conducted fraudulent unauthorized trades in the account it managed for them in violation of the Virginia Securities Act § 13.1-522(a). Their claim against Sears is based solely on Sears' status as a controlling person of Dean Witter. Virginia Securities Act § 13.1-522.C. Plaintiffs attribute no fraudulent conduct to Sears and, all agree, no recovery against Sears is possible unless plaintiffs first prove their claim against Dean Witter.

In enacting the Federal Arbitration Act, Congress created national substantive law governing all questions of the validity and enforceability of arbitration agreements within its scope. *Genesco, Inc. v. T. Kakiuchi & Co., Ltd.*, 815 F.2d 840, 845 (2d Cir. 1987) (citing *Mitsubishi*

Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 626 (1985)); *see also Moses H. Cone*, 460 U.S. at 24; *Varley v. Tarrytown Associates, Inc.*, 477 F.2d 208, 209 (2d Cir. 1973). Hence, whether plaintiffs are bound by the arbitration clause of the contract with Dean Witter is a matter of federal law, which incorporates generally accepted principles of contract law. *See Genesco*, 815 F.2d at 845 (citing *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 404-05 (1967)). Accordingly, section 2 of the Act provides that arbitration provisions "shall be valid, irrevocable and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2.

Section 3 of the Act provides:

> § 3. Stay of proceedings where issue therein referable to arbitration
>
> If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration.

A commonsense reading of this section suggests that if there is a federal action "upon" an "issue referable to arbitration" by the terms of an arbitration agreement,

then the federal court must "stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement."

The relevant arbitration clause agreed to by plaintiffs and Dean Witter states that "any controversy between [Dean Witter] and the undersigned [plaintiffs] arising out of or relating to this contract or the breach thereof shall be settled by arbitration." Plaintiffs do not claim that the dispute in *McCowan II*, does not "aris[e] out of" or "relat[e] to" the contract containing the arbitration clause, nor could they. Indeed, it is Dean Witter's alleged mishandling of the very account opened in connection with the parties' contract that is at issue in both *McCowan I* and *McCowan II*. The district court determined as much when it granted the stay in *McCowan I* of federal claims based on the same allegations of misconduct—a decision which was clearly correct in light of *Shearson American Express v. McMahon*, 482 U.S. 220 (1987). Rather, plaintiffs assert that there exists no arbitrable "controversy" between them and Dean Witter in *McCowan II* because no judgment is sought against Dean Witter in that action.

We believe that the absence of a request for relief against Dean Witter does not determine whether a controversy exists between Dean Witter and plaintiffs, and that the district court erred when it held that the absence of a request for a judgment against Dean Witter, barred Dean Witter from invoking the agreement. Althougn fashioned as two separate lawsuits, there is in reality a single "controversy" at issue—as that term would have been understood by the contracting parties—giving rise to claims under three separate laws: the 1934 Act, RICO and the Virginia Securities Act. The first two demand a

money judgment from Dean Witter; the third requires a showing of liability against Dean Witter as a predicate to recovery against Sears, but demands no monetary judgment from Dean Witter. Dean Witter's contractual right to arbitrate "any controversy" arising out of or relating to the contract between the parties would be seriously impaired if *McCowan II* were not stayed pending arbitration. Under these circumstances, we believe that Dean Witter has a right to the mandatory stay afforded by section 3 of the Act.

Dean Witter is involved in a "controversy," as that term is commonly understood, with plaintiffs over its management of their account. *See* Webster's Third New International Dictionary 497 (1981) ("the act of disputing or contending . . . a cause, occasion, or instance of disagreement or contention"). Even if the parties intended to arbitrate controversies defined as "a suit in law or equity," *McCowan II* is such a suit, *see* Black's Law Dictionary 298 (4th ed. 1979), and Dean Witter as a named defendant would be obliged, if the suit were to proceed, to file an answer and bear the costs of its defense.

Moreover, the presence of the *McCowan I* federal claims before the arbitrator weighs heavily in favor of a stay of the state law claims in *McCowan II*. If *McCowan II* were allowed to proceed against Dean Witter in federal court, Dean Witter's right to arbitrate the federal claims already referred to arbitration in *McCowan I* would be impaired since any issues determined against Dean Witter in court proceedings in *McCowan II* could have collateral estoppel effect on the arbitration. *See Dickson v. Heinold Securities, Inc.*, 661 F.2d 638, 644 (7th Cir. 1981); *Mansbach v. Prescott, Ball, Turben*, 598

F.2d 1017, 1031 (6th Cir. 1979) (principles of collateral estoppel prevent relitigation of issues in arbitration that have already been decided in federal court); *N.Y.S. Ass'n for Retarded Children v. Carey*, 456 F. Supp. 85, 96 (E.D.N.Y. 1978), *aff'd* 596 F.2d 27 (2d Cir. 1979); *J.D. Marshall Intern, Inc. v. Redstart, Inc.*, 656 F. Supp. 830, 834 (N.D. Ill. 1987) (prior federal proceeding has full collateral estoppel and res judicata effects on subsequent arbitration). While section 13.1-522(a) of the Virginia Securities Act differs from Rule 10b-5 of the 1934 Act by placing the burden of disproving scienter on the defendant rather than requiring the plaintiff to prove it, and by making negligent as well as intentional misrepresentations actionable, *see* 4 A. Bromberg & L. Lowenfels, *Securities Fraud & Commodities Fraud*, § 8.4, pp. 204.1, 204.146, 204.170 (1989), in other respects certain elements of the state and federal offenses appear to be the same, including a failure to disclose, materiality and causation. *Id.* at § 8.1, p. 195. According to Professor Loss, the Virginia statute, like other state fraud statutes modeled after section 101 of the Uniform Securities Act, "is substantially the SEC's rule 10b-5." *See* L. Loss, *Commentary on the Uniform Securities Act*, 6 (1976). Thus, the preclusive effect of court action in *McCowan II* in the *McCowan I* arbitration is potentially substantial and significant.

Our interpretation of the arbitration agreement to include the *McCowan II* claims against Dean Witter furthers and is supported by the "liberal federal policy favoring arbitration." *Moses H. Cone*, 460 U.S. at 24. "The legislative history of the Act establishes that the purpose behind its passage was to ensure judicial enforcement of privately made agreements to arbitrate." *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213, 219

(1985); *see also Mitsubishi Motors Corp.*, 473 U.S. at 625. Thus, we conclude that the *McCowan II* claims against Dean Witter must be stayed pending arbitration under section 3 of the Arbitration Act.

Sears moved in the district court for a stay of *McCowan II* as an exercise of the district court's discretion at the same time Dean Witter moved pursuant to Arbitration Act section 3. After the district court denied both motions, Sears moved for a section 3 stay claiming a right to enforce the arbitration agreement as a third party beneficiary of the agreement or based on its status as a "controlling person" of Dean Witter. In view of our holding that Dean Witter is entitled to a mandatory section 3 stay, we need not determine whether Sears also has such a right. The practical effect of the stay as to Dean Witter, an indispensable party in *McCowan II*, is that the suit against Sears, which is wholly dependent on the claim against Dean Witter, cannot proceed.

Judgment reversed.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

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HORACE D. McCOWAN, JR. and
SARAH E. McCOWAN,

Plaintiffs,

-against-

SEARS, ROEBUCK AND CO., and
DEAN WITTER REYNOLDS, INC.,

Defendants.

----------x

OPINION

87 Civ. 2336
(RLC)

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CARTER, District Judge

Defendants Dean Witter Reynolds, Inc. ("Dean Witter") and Sears, Roebuck & Co. ("Sears") bring a motion to dismiss or, in the alternative, to stay all claims asserted against them by plaintiffs Horace D. McCowan, Jr. and Sarah E. McCowan (together, the "the plaintiffs"). The plaintiffs charge the defendants with violation of the Virginia Securities Act. This court has diversity jurisdiction pursuant to 28 U.S.C. 1332 (1976).

I.

This is the court's third disposition in this litigation and familiarity with prior opinions is assumed. We briefly review the history of this litigation to help further the understanding of the instant determination.

On October 31, 1986, the plaintiffs brought suit in the Southern District of New York against Dean Witter alleging violations of the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. §§ 1961-1968 ("RICO"), the Securities Act of 1933 (the "1933 Act"), and the Securities Exchange Act of 1934 (the "1934 Act") ("*McCowan I*"). On December 31, 1986, the plaintiffs filed a diversity suit in the Eastern District of Virginia against both Dean Witter and Sears alleging "controlling person" liability against Sears pursuant to the Virginia Securities Act, Va. Code Ann. § 13.1-501 *et seq.* ("*McCowan II*"). Because both cases arise out of the same facts and involve the same subject matter, Judge James R. Spencer of the Eastern District of Virginia ordered in April, 1987 that *McCowan II* be transferred to this district. In May, 1987, the actions were consolidated.

In an opinion dated December 21, 1987, *McCowan v. Dean Witter Reynolds, Inc.*, 682 F. Supp. 741 (S.D.N.Y. 1987) (Carter, J.), the court referred the RICO claims and the claims arising under the 1934 Act to arbitration. The court found that the claims arising under the 1933 Act were deficiently pleaded and dismissed such claims with leave to replead. The decision on the defendants' motion to dismiss the Virginia state law claim was deferred until the plaintiffs had repleaded their 1933 Act claims. An amended complaint was filed on January 19, 1988, under the *McCowan I* caption only. In a slip opinion, Fed. Sec.

L. Rep. (CCH) ¶ 94,423 (S.D.N.Y. April 11, 1989), the court held that there was no private right of action under § 17(a) of the 1933 Act and that § 12(2) of the 1933 Act is inapplicable to post-distribution transactions, and accordingly dismissed those counts of the plaintiffs' amended complaint. The only claim left for disposition is the Virginia state law claim contained in *McCowan II*.

II.

Defendant Dean Witter is indirectly owned by defendant Sears.[1] Although Sears owns no Dean Witter stock directly, it is the sole owner of Dean Witter Financial Services Inc., which is the sole owner of Dean Witter.

Early in 1985, the plaintiffs established an account with Dean Witter including a non-discretionary securities account. In numerous transactions during the months of January through October, 1985, Dean Witter, as broker for the plaintiffs, sold them numerous shares of several securities, including an aggregate of 219,000 shares of Hawkeye Bancorporation ("Hawkeye") and 120,000 shares of First Interstate of Iowa.

To make the sales, Dean Witter sold other shares in the plaintiffs' securities account, used the plaintiffs' cash funds, and incurred margin debt for the plaintiffs. Although the securities account was a non-discretionary account, Dean Witter made each sale without prior approval from the plaintiffs and without disclosing to the plaintiffs material information known to Dean Witter concerning the sale, the shares, the issuers and Dean Witter's opinions regarding such stock. Dean Witter conducted each transaction with the plaintiffs for Dean Witter's own account as a principal and dealer without the plaintiffs' prior consent, merely sending an unauthorized confirmation for each transaction to the plaintiffs.

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[1] All facts are those set forth in the plaintiffs' complaint and affidavit. These facts have not yet been proven or stipulated to between the parties, but for the purposes of this motion the court presumes all of the plaintiffs' allegations to be true. *Bloor v. Carro, Spanbock, Londin, Rodman & Fass*, 754 F.2d 57, 61 (2d Cir. 1985).

Dean Witter mailed the plaintiffs monthly statements from January to October, 1985. Such statements contained, among other things, the "market value," current "portfolio value," and "net equity" value for each of the securities in the securities account. Dean Witter represented that the "market value" and "portfolio value" were determined by a quotation service appraisal. Dean Witter represented that the plaintiffs' securities account had a net equity value of over $1.5 million as of June 30, 1985, but reported that it had dropped to a little over $1 million as of October 31, 1985.

After a drop in the value of the securities account, plaintiffs directed Dean Witter to liquidate the securities account in November, 1985. Dean Witter did not complete liquidation until January, 1986, and failed to disclose to the plaintiffs that it did not intend to execute their order to liquidate immediately. During the time of liquidation, Dean Witter acted as a market maker for Hawkeye shares, purchasing, selling, offering, bidding for and owning a significant number of Hawkeye shares. Moreover, during this period, Dean Witter traded in Hawkeye shares as a principal for its own account. After liquidation was completed, and all margin debt and costs were paid, the net return to the plaintiffs was $294.

At the time of each transaction for the plaintiffs' securities account, Dean Witter was familiar with and had peculiarly within its knowledge or available to it extensive, current, and material information concerning each transaction. Dean Witter misled the plaintiffs by recklessly, negligently, or willfully concealing, or failing fully and fairly to disclose to the plaintiffs information then known to Dean Witter and material to an informed investment decision to purchase such shares.

The defendants move for dismissal of the complaint pursuant to Rule 12(b)(6), F.R.Civ.P., on the grounds that the complaint fails to state a claim for relief against Sears under the Virginia Securities Act. The defendants also move for dismissal on the ground that the complaint fails to allege fraud with the particularity required pursuant to Rule 9(b), F.R.Civ.P. Regarding

Dean Witter, the defendants move for dismissal on the grounds that the complaint seeks no relief against Dean Witter as required by Rule 8(a)(3), F.R.Civ.P. Finally, the defendants request that if this action is not dismissed, the court stay proceedings pending the outcome of the previously ordered arbitration between the plaintiffs and Dean Witter.

III.

The plaintiffs' complaint is predicated on alleged violations of the Virginia Securities Act, Section 13.1-501 *et seq.* of the Virginia Code Annotated (1977) (hereafter, "§ ____" or, collectively, the "Virginia Act"). Section 13.1-522(a) provides in relevant part:

> Any person who. . .[s]ells a security by means of an untrue statement of a material fact or any omission to state a material fact necessary in order to make the statement made, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission, shall be liable. . .

Section 13.1-522(b) describes the liability of a controlling person as follows:

> Every person who . . . directly or indirectly controls any person [liable under §13.1-522(a),] shall also be liable jointly and severally with and to the same extent as the person so liable, unless the person who so . . . controls sustains the burden of proof that he did not know, and in the exercise of reasonable care could not have known of the existence of the facts by reason of which the liability is alleged to exist.[2]

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[2] This section was amended in 1987 and re-numbered as § 13.1-522.C. It now states in full:

(Footnote continued)

The plaintiffs claim that Sears is such a controlling person with respect to Dean Witter.

A.

As a threshold matter, it is clear that § 13.1-522(a)(2) expressly creates a private right of action for fraudulent sales for a purchaser of securities. Section 13.1-522(a)(2) states in relevant part, "[a]ny person who [sells a security and is guilty of a violation or sells a security by means of fraud] *shall be liable to the person purchasing such security* from him who may sue either at law or in equity to recover the consideration paid for such security. . ." (emphasis added).[3] *See also Merchant v. Oppenheimer & Co., Inc.*, 568 F. Supp. 639, 642 (E.D. Va. 1983), *aff'd in part, rev'd in part* 739 F.2d 165 (4th Cir. 1984).

Furthermore, § 13.1-522(a)(2) expressly protects every purchaser defrauded in a sale of securities. Unlike § 12(2) of the 1933 Act, § 13.1-522(a)(2) applies to post-distribution trading as well as to initial distributions. It is not necessary under § 13.1-522(a)(2) for the sale to involve a prospectus or be part of

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> Every person who directly or indirectly controls a person liable under subsection A or B of this section, including every partner, officer, or director of such a person, every person occupying a similar status or performing similar functions, every employee of such a person who materially aids in the conduct giving rise to the liability, and every broker-dealer, investment advisor, investment advisor representative or agent who materially aids in such conduct shall be liable jointly and severally with and to the same extent as such person, unless able to sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of the existence of the facts by reason of which the liability is alleged to exist. There shall be contribution as in cases of contract among the several persons so liable.

Va. Code Ann. § 13.1-522.C (1989).

[3] Although § 17(a) of the 1933 Act, 15 U.S.C. § 77q(a), is virtually identical to the portion of § 13.1-522(a)(2) which describes the prohibited fraudulent conduct, § 17(a) contains no express private right of action.

an initial distribution. In this sense, the Virginia Act covers areas from both the 1933 Act and the 1934 Act. *Gurley v. Documation, Inc.*, 674 F.2d 253, 259 (4th Cir. 1984) ("Virginia's blue sky law shares with § 10b of the 1934 Act the central purpose of protecting investors from fraud in the securities markets."); Loss, Securities Regulation (1989) at 51 (The section of the Uniform Securities Act on which § 13.1-522(a) was modeled is "based on Rule 10b-5 [and] outlaws fraudulent practices in connection with the sale or purchase of a security."); Loss, Commentary on the Uniform Securities Act (1976) at 6 ("the Virginia Act is substantially Rule 10b-5"). It has been held specifically that there is a private right of action under the Virginia Act for trading done by brokers. *Merchant v. Oppenheimer & Co., Inc., supra*, 568 F. Supp. at 642.

B.

The defendants argue that although Sears is effectively the sole shareholder of Dean Witter, it is not a "controlling person" within the meaning of the Virginia Act.[4] There are no Virginia cases interpreting "controlling person,"[5] but other cases and

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[4] In an effort to support their position, the defendants argue that the 1987 amendment to § 13.1-522(b) (currently numbered § 13.1-522.C) shows that the Virginia legislature never intended for sole shareholders to be included in the definition of "controlling person." The defendants' argument misinterprets the 1987 amendment. This amendment does not change the law with regard to controlling persons themselves, but instead makes liable partners, officers, and directors of controlling persons and employees, broker-dealers, investment advisors, investment advisor representatives and agents of controlling persons if such persons materially aided in the conduct of the controlling person.

[5] The defendants cite *Kennedy v. Nicastro*, 503 F. Supp. 1116, 1121 (N.D.Ill. 1980) and *Hokama v. E.F. Hutton & Co.*, 566 F. Supp. 636, 646-47 (C.D. Cal. 1983) in support of their position that absolute stock ownership does not establish control. These cases are not persuasive, however, because they were dismissed for inadequate pleading. The defendants also cite *Wool v. Tandem Computers Inc.*, 818 F.2d 1433, 1441 (9th Cir. 1987). As *Tandem Computers*

(Footnote continued)

regulations define "control" to mean the power to control. 17 C.F.R. § 240.12b-2 (1986) (S.E.C. regulation defining control as ". . . the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract or otherwise."); *Safeway Portland Employees' Federal Credit Union v. C.H. Wagner & Co.*, 501 F.2d 1120, 1124 n.17 (9th Cir. 1974) (citing the SEC definition). It is obvious that Sears had the power to control Dean Witter. As the sole shareholder of Dean Witter, Sears could, for example, remove and replace Dean Witter's officers or directors, amend its charter, sell its assets, or merge it into another company. As the sole shareholder of Dean Witter, Sears is a "controlling person" for the purposes of § 13.1-522(b).

C.

The defendants argue that the plaintiffs' allegations that Sears was a "controlling person" are insufficient because they do not allege that Sears was a culpable participant in the alleged fraud. The plaintiffs argue that it is only necessary to plead that Sears had control, all else being an affirmative defense. Based on an analogy to Section 20(a) of the 1934 Act ("Section 20(a)"), the defendants maintain that they are not required to come forward with their good faith defense that they did not know and could not have known of the fraud until the plaintiffs allege culpable participation.[6]

A decision regarding necessary allegations cannot be based on an analysis of Section 20(a), however, because § 13.1-522(b)

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correctly observed, ordinarily holding the position of officer of a company is insufficient to presume control. This case is not on point, however, since there are clear and obvious differences between the power of an officer of a company as in *Tandem Computers* and the power of a company's sole shareholder as in this case.

[6] Although it has not been held that these two statutes are identical, they were treated as identical in *Walker v. Cardinal Savings and Loan Association*, 690 F. Supp. 494 (E.D. Va. 1988).

differs from § 20(a).[7] Section 20(a) provides liability for "[e]very person who, directly or indirectly, controls any person liable. . ." Section § 13.1-522(b), on the other hand, provides liability for "[e]very person who materially participates or aids in a sale made by any person liable. . .or who directly or indirectly controls any person so liable. . ." A facial comparison of these two statutes thus shows that while § 20(a) only imposes liability on controlling persons, § 13.1-522(b) imposes liability on both controlling persons and on persons who materially participate or aid.[8]

The history of the Virginia Act sheds further light on the two kinds of liability found in § 13.1-522(b). Virginia's blue sky law has imposed liability on those who "participated or aided" in securities fraud since 1928.[9] It was not until 1956 that Virginia

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[7] Even if the Virginia Act was analogous to § 20(a) it is not clear that it is necessary to allege that Sears is a culpable participant. Although this allegation would be required in other circuits, *see, e.g., Wool v. Tandem Computers Inc., supra*, 818 F.2d at 1440, authority in this circuit regarding pleading requirements for § 20(a) is mixed. It is clear that in enacting § 20(a) Congress intended to impose liability only on those "who fall within its definition of control and who are in some meaningful sense culpable participants in the fraud perpetrated by controlled persons." *Lanza v. Drexel & Co.*, 479 F.2d 1277, 1299 (2d Cir. 1973). What is less clear is whether a plaintiff must allege and prove culpable participation or whether culpable participation is assumed unless the defendant comes forward with a good faith defense. Although it has been said that "[i]n this Circuit "good faith" is recognized as a defense under [§ 20(a)]," *Terra Resources I. v. Burgin*, 664 F.Supp. 82, 88 (S.D.N.Y. 1987) (Sweet, J.), citing *Marbury Management, Inc. v. Kohn*, 629 F.2d 705, 716 (2d Cir. 1975), *cert. denied*, 449 U.S. 1011 (1980), it has also been held that it is necessary to allege culpable participation. *O'Connor & Assoc. v. Dean Witter Reynolds, Inc.*, 529 F. Supp. 1179, 1194-95 (S.D.N.Y. 1981) (Lasker, J.); *Gordon v. Burr*, 506 F.2d 1080, 1086 (2d Cir. 1974).

[8] Section 13.1-522(b) also differs from § 410(b) of the Uniform Securities Act on which it was based. Section 410(b) provides liability for "[e]very person who directly or indirectly controls a seller liable. . ." It makes no mention of liability for those who "participate or aid."

[9] Chapter 15 of Virginia's blue sky law, Va. Acts 1928, ch. 329, pp. 1392-93, provided in relevant part:

(Footnote continued)

law made controlling persons also liable.[10] It is reasonable to conclude from this legislative history that participation is not always required for controlling person liability because such requirement would make the 1956 controlling person liability amendment meaningless since participants were already liable. From this it follows that control and participation can each serve as an independent basis from which liability can be imposed. Because participation is not required to prove liability based on control under § 13.1-522(b), it is obviously not required to be pleaded.

D.

The defendants claim that the plaintiffs' allegations of fraud have not been pleaded in accordance with Rule 9(b), F.R.Civ.P., which provides:

> In all averments of fraud or mistake, the circumstances constituting fraud or mistake shall be stated with particularity. Malice, intent, knowledge, and other condition of mind of a person may be averred generally.

> the person making such sale or contract for sale, and every agent of or for such seller who shall have participated or aided in any way in making such sale, shall be jointly and severally liable to such purchaser. . .

This was codified in 1930 as Va. Code Ann. § 3848(61) (1930).

[10] 1956 Va. Acts 428, codified as Va. Code Ann. § 13.1-552(b) (1950) provided in relevant part:

> Every person who materially participates or aids in a sale made by any person liable under subsection (a), or who directly or indirectly controls any person so liable, shall also be liable jointly and severally with and to the same extent as the person so liable, unless
>
> the person who so participates, aids or controls sustains the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of the existence of the facts by reason of which the liability is alleged to exist.

Specifically, the defendants maintain that the plaintiffs have failed to allege sufficiently the material misrepresentations or omissions, scienter, and reliance and causation.

It is clear that Rule 9(b) imposes more severe pleading requirements than are generally needed under Rule 8 which states that pleadings should contain a "short and plain" statement of the claim or defense and each averment should be "simple, concise and direct." Rule 9 does not render the general principles of Rule 8 inapplicable and, when necessary, "F.R.Civ.P. 9(b) must be reconciled with F.R.Civ.P. 8(a)(2)." *Denny v. Barber*, 576 F.2d 465, 467 (2d Cir. 1978)

In assessing the complaint, it is necessary to keep in mind that Rule 9(b) serves several important purposes. First, it assures the defendant of "fair notice of what the plaintiff's claim is and the grounds upon which it rests." *Denny v. Barber, supra*, 576 F.2d at 469. Second, the requirement of specificity gives defendants some assurance that their reputations will not be damaged by unsubstantiated charges of fraudulent behavior. *Ross v. A.H. Robins Co.*, 607 F.2d 545, 557 (2d Cir. 1979), *cert. denied*, 446 U.S. 946 (1980). Finally, and of particular importance in the securities context, requiring specificity prevents strike suits filed solely for their settlement value. *Decker v. Massey-Ferguson*, 681 F.2d 111, 115 (2d Cir. 1982).

The defendants first argue that the plaintiffs have not alleged specific facts to support their claims of misrepresentation and omission. As a general rule, a plaintiff must "specify the time, place, speaker, and sometimes even the content of the alleged misrepresentations." *Luce v. Edelstein*, 802 F.2d 49, 54 (2d Cir. 1986). The plaintiffs have specified the relevant time period, the stocks in question, and the content of the alleged misrepresentations. The plaintiffs have also clearly set out the information they are claiming the defendants knew but omitted to report. The plaintiffs' allegations meet the Rule 9 standard in that they give the defendants "fair notice of what [the plaintiffs'] claim is and the grounds upon which it rests." *Denny v. Barber, supra*, 576 F.2d at 469.

The defendants next argue that the plaintiffs fail to allege scienter sufficiently. However, the plaintiffs are not required to allege or prove scienter for a violation of § 13.1-522.[11] This section imposes liability on each person "who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known [of the false representation or omission]." It is unnecessary for a plaintiff to allege or prove scienter since the defendant is liable unless he can prove reasonable conduct resulting in actual lack of knowledge.

It is logically required that scienter not be an element of § 13.1-522 since the statutory "reasonable care" affirmative defense is inconsistent with the element of scienter. If scienter was an element of § 13.1-522, then the "reasonable care" affirmative defense included within that section would be pointless as well as violate basic legal principles. Such defense would be pointless because if a defendant proved lack of knowledge and reasonable care, then it would be impossible for the plaintiff to prove all the elements of the offense. In this situation it would be unnecessary for a defendant to have a statutory affirmative defense. Furthermore, if scienter was an element of § 13.1-522, the "reasonable care" defense would be wrong as a matter of basic legal principle. Absent statutory directive, the burden is on a plaintiff to prove each element of an offense, not on a defendant to disprove it.

Other courts construing statutes similar to § 13.1-522 have reached the same conclusion. *American General Insurance v. Equitable General Corp.*, 493 F.Supp. 721 (E.D.Va. 1980) (similar analysis regarding a Texas statute almost identical to § 13.1-522); Bromberg & Lowenfels, Securities Fraud & Commodities Fraud,

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[11] In any event, the plaintiffs have met their scienter pleading requirement. As the defendants themselves acknowledge, the plaintiffs have made scienter allegations of recklessness, in the alternative, in paragraphs 18, 21, and 22 of their complaint. Recklessness satisfies the scienter requirement, at least in cases such as this where the defendant owed the plaintiff a fiduciary duty. *Rolf v. Blyth, Eastman Dillon & Co., Inc.*, 570 F.2d 38, 44 (2d Cir. 1978), *cert. denied*, 439 U.S. 1039 (1978).

§ 8.4(210), pp. 204.1-204.2 (1988) (Uniform Securities Act upon which § 13.1-522 was based does not require scienter).

Finally, the defendants argue that the plaintiffs fail to allege reliance and causation. However, in non-disclosure cases it is not necessary to allege and prove reliance and causation. As the Supreme Court has held in a case alleging primarily non-disclosure,

> proof of reliance is not a prerequisite to recovery. All that is necessary is that the facts withheld be material in the sense that a reasonable investor might have considered them important in the making of this decision. [citations omitted] This obligation to disclose and this withholding of a material fact establish the requisite element of causation in fact. *Affiliated Ute Citizens of Utah v. United States*, 406 U.S. 128, 92 S.Ct. 1456, 1472, 31 L.Ed. 2d 741 (1972).

In the case at hand, the essence of the plaintiffs' complaint is that the defendants failed to disclose material facts to them. Therefore it is not necessary that the plaintiffs allege and prove reliance.

E.

The defendants argue pursuant to Rule 8(a)(3), F.R.Civ.P.,[12] that Dean Witter should not be a party to this action because the plaintiffs seek no relief from Dean Witter. The plaintiffs, on the other hand, argue that Dean Witter is an indispensable party within the meaning of Rule 19, F.R.Civ.P.[13] The plaintiffs claim against Sears is a derivative one based on its "control" of Dean Witter as a wholly-owned subsidiary. Although Sears'

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[12] Rule 8(a)(3) provides in relevant part: "A pleading which sets forth a claim for relief . . . shall contain a demand for judgment for the relief the pleader seeks."

[13] Rule 19(a) provides in relevant part: "A person . . . shall be joined as a party in the action . . . if the person claims an interest relating to the subject of the action . . ."

control of Dean Witter, as well as its knowledge of the alleged violation are questions that involve primarily Sears, the alleged underlying violation in this case involves Dean Witter. Most of the allegations in the complaint are directed at the activity of Dean Witter and liability exists for Sears only if the plaintiffs demonstrate that Dean Witter violated the Virginia Act. In sum, almost everything that is in controversy is so as a result of the actions of Dean Witter. In light of these facts, Dean Witter is clearly an indispensable party to this action.[14] *See Freeman v. Northwest Acceptance Corp.*, 754 F.2d 553 (5th Cir. 1985) ("[subsidiary] was more than an active participant. . . it was the primary participant" and therefore should be joined) and cites therein.

F.

The defendants have requested a stay of this proceeding pending the outcome of the court-ordered arbitration between the plaintiffs and Dean Witter. Whether to stay litigation involving non-arbitrating parties pending the outcome of an arbitration is a decision left to the district court as a matter of its discretion to control its docket. *Moses H. Cone Memorial Hosp. v. Mercury Const.*, 460 U.S. 1, 20 n.23, 103 S.Ct. 927, 74 L.Ed. 2d 765 (1983). Although both this case and the arbitration center around the conduct of Dean Witter, they proceed under statutes which have different elements and therefore the outcome of one proceeding will not be dispositive of the other. Accordingly, "the concern for speedy resolution suggests that neither should be delayed" and therefore no stay will be granted. *Chang v. Lin*, 824 F.2d 219, 223 (2d Cir. 1987) (quoting *Dean Witter Reynolds Inc. v. Byrd*, 470 U.S. 213, 221, 105 S.Ct. 1238, 84 L.Ed. 2d 158 (1985)).

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[14] None of the cases cited by the defendants are persuasive. In such cases, the party seeking dismissal either had no significant involvement with the dispute being litigated or the plaintiff did not adequately state a claim against the defendant. In contrast, in the case at hand, Dean Witter is the primary actor in the dispute and the plaintiffs have adequately alleged Dean Witter's violation of Virginia law.

IV.

In conclusion, for the reasons stated above, the defendants' motions for dismissal of the complaint pursuant to Rule 12(b)(6), F.R.Civ.P.; for dismissal of the complaint as to Dean Witter; and for a stay of the proceedings pending arbitration are denied. The defendants are directed, pursuant to Rule 12(a), F.R.Civ.P., to answer the plaintiffs' complaint within 20 days after receiving this opinion.

IT IS SO ORDERED.

Dated: New York, New York
October 12, 1989

/s/ Robert L. Carter

Robert L. Carter
U.S.D.J.

HORACE D. McCOWAN, JR., et al.
v.
SEARS, ROEBUCK AND CO., et al.

87 Civ. 2336 (RLC)

ENDORSEMENT

The defendants Sears, Roebuck and Co. ("Sears") and Dean Witter Reynolds, Inc. ("Dean Witter") move pursuant to Local Rule 3(j) of the Civil Rules of the United States District Courts for the Southern and Eastern Districts of New York for reargument of their earlier motion requesting dismissal or stay of all claims asserted against them by the plaintiffs, and, alternatively, for clarification of the court's denial of a stay of these proceedings pending the outcome of arbitration.

The defendants' motion for reargument is denied. The "'only proper ground for a motion for reargument is that the court overlooked "matters or controlling decisions" which, had they been considered, might reasonably have altered the result reached by the court.' " *United States v. International Business Machines Corp.*, 79 F.R.D. 412, 414 (S.D.N.Y. 1978) (Edelstein, J.) (quoting *United States v. International Business Machines Corp.*, 69 Civ. 200 (DNE), slip op. at 2 (S.D.N.Y. Oct. 10, 1975)); *Wm. Passalacqua Bldrs. v. Resnick Developers South*, 611 F. Supp. 281, 283 (D.C.N.Y. 1985) (Edelstein, J.). The court has carefully considered the facts of this case, the relevant legal authority, and all submissions by the defendants in making its determination. The defendants have not indicated that they have any new material to bring to the attention of the court and, therefore, reargument would serve no purpose.

In response to the defendants' request for clarification, the court affirms its earlier ruling denying the defendants' motion for a stay pending the outcome of arbitration. As a subsidiary of Sears and the primary actor in this case, Dean Witter is an indispensable party within the meaning of Rule 19, F.R.Civ.P., and, accordingly, is properly joined in this action. *Freeman v. Northwest Acceptance Corp.*, 754 F.2d 553, 559 (5th Cir. 1985)

and cites therein. The court recognizes that Dean Witter has an arbitration agreement with the plaintiffs. However, the dispute in this case is between the plaintiffs and Sears, and no judgment is, or can be, demanded of Dean Witter. The plaintiffs have made allegations against Sears which are properly adjudicated in this forum, and they are entitled to timely consideration of their claims.

At the defendants' request, their deadline to answer the complaint is extended until November 16, 1989.

IT IS SO ORDERED

Dated: November 8, 1989
New York, New York

/s/ Robert L. Carter

Robert L. Carter
U.S.D.J.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

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HORACE D. McCOWAN, JR. and
SARAH E. McCOWAN,

Plaintiffs,

-against-

SEARS, ROEBUCK AND CO., and
DEAN WITTER REYNOLDS, INC.,

OPINION
87 Civ. 2336
(RLC)

Defendants.

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CARTER, District Judge

Defendant Sears, Roebuck and Co. ("Sears") moves pursuant to the Federal Arbitration Act, 9 U.S.C. § 3 (1970), to stay all claims asserted against it in the above-captioned action pending arbitration between plaintiffs and defendant Dean Witter Reynolds ("Dean Witter") on the grounds that it is a third-party beneficiary to an arbitration agreement made between plaintiffs and Dean Witter.

I.

This case has been the subject of numerous motions to date, familiarity with which is presumed, and it is therefore unnecessary to provide any more than a thumbnail sketch of the background relevant to this motion.[1] Although started as two separate lawsuits in different districts,[2] in May, 1987, the two cases were consolidated in this court. In an opinion dated December 21, 1987, *McCowan v. Dean Witter Reynolds, Inc.*, 682 F. Supp. 741 (S.D.N.Y. 1987) (Carter, J.), *app. dismissed*, 889 F.2d 451 (2d Cir. 1989), the court referred the RICO claims and the claims arising under the Securities Exchange Act of 1934 to arbitration.[3] The court found that the claims arising under the Securities Act of 1933 ("1933 Act") were deficiently pleaded and dismissed such claims with leave to replead. The decision on the defendants' motion to dismiss the Virginia state law claims was deferred until the plaintiffs had repleaded their 1933 Act claims. An amended complaint was filed on January 19, 1988, and in an opinion dated April 11, 1989, Fed. Sec. L. Rep. (CCH)

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[1] For a complete background of the case, *see*, 682 F. Supp 741 (S.D.N.Y. 1987) (Carter, J.); Fed. Sec. L. Rep. (CCH) ¶ 94,423 (S.D.N.Y. April 11, 1989); and 722 F. Supp. 1069 (S.D.N.Y. 1989).

[2] *McCowan v. Dean Witter Reynolds, Inc.*, No. 86 Civ. 8398 (RLC) was initiated in this district. *McCowan v. Sears, Roebuck and Co., et al.*, No. 87 Civ. 2336 (RLC), was transferred from the Eastern District of Virginia and consolidated with the case already in this district.

[3] Subsequent to the court's decision, the Supreme Court overruled prior precedent and held that agreements to arbitrate claims brought under the 1933 Act are enforceable. *Rodriguez de Quijas v. Shearson/American Express, Inc.*, ___ U.S. ___, 109 S. Ct. 1917 (1989).

¶ 94,423, the court held that there was no private right of action under § 17(a) of the 1933 Act and that § 12(2) of the 1933 Act is inapplicable to post-distribution transactions, and accordingly dismissed those counts of the plaintiffs' amended complaint.

By this time, the only claims left in this case were the Virginia state law claims, and on October 12, 1989, the court denied defendants' motion for dismissal thereof. *McCowan v. Sears, Roebuck and Co.*, 722 F. Supp. 1069. In the same opinion, the court found Dean Witter to be an indispensable party within the meaning of Rule 19, F.R.Civ. P., and denied defendants' motion for a stay of the proceedings pending arbitration. Defendants moved for reargument as to the denial of the stay, and this was denied in an endorsement dated November 8, 1989.

Defendant Sears once again moves for a stay pending arbitration.*

II.

Sears has previously moved for a stay and for re-argument, and did not raise on either occasion the third-party beneficiary theory which it now suggests. Furthermore, Sears does not offer any explanation as to why it did not raise this theory in its previous motions.

As a general rule, parties must raise all arguments regarding a particular issue at the same time. *Christianson v. Colt Indus. Operating Corp.*, ____ U.S. ____, 108 S. Ct. 2166, 2177 (1988). It is a basic principle that, absent a decision which was clearly erroneous and which would work a manifest injustice, once a court has considered and decided an issue, "that decision should continue to govern the same issue[] in subsequent stages in the same case." *Arizona v. California*, 460 U.S. 605, 618 (1983), *reh. denied*, 462 U.S. 1146. *See also, White v. Murtha*, 377 F.2d 428, 432 (5th Cir. 1967). "This rule of practice promotes the finality and efficiency of the judicial process by 'protecting against

* Defendant Dean Witter, having appealed the court's previous rulings denying a stay, does not join in this current motion.

the agitation of settled issues.' " *Christianson v. Colt Indus. Operating Corp.*, ____ U.S. ____, 108 S. Ct. at 2177 (quoting 1B J. Moore, J. Lucas, & T. Currier, Moore's Federal Practice ¶0.404[1], p. 118 (1984)). Sears' failure to make its current argument at the time of its first motion for stay is in itself sufficient grounds to deny this motion. Nevertheless, because this rule is permissive rather than mandatory, *id.* at 2178, the court will evaluate Sears' motion on the merits.

Sears argues that, as a shareholder of Dean Witter,[5] it is an intended beneficiary of any contract Dean Witter may make and, as such, it may enforce the arbitration agreement.[6] It is undisputed that based on general contract principles an arbitration agreement may be enforced by or against a party who did not personally sign the arbitration contract, *Fisser v. International Bank*, 282 F.2d 231, 233 (2d Cir. 1960), and that only an intended beneficiary, as opposed to an incidental beneficiary, has enforcement rights. *Fourth Ocean Putnam v. Interstate Wrecking*, 66 N.Y.2d 38, 43, 495 N.Y.S.2d 1, 4 (1985); Restatement (Second) of Contracts § 304 (1986).

The sole question then, is whether Sears was an intended beneficiary or an incidental beneficiary of the arbitration agreement made between Dean Witter and the plaintiffs. To enforce the arbitration agreement as a third-party beneficiary, Sears must show that it was " 'the real promisee,' that is, '[the promisee in fact although not in form.' " *Worldwide Sugar Co. v. Royal Bank of Canada*, 609 F. Supp. 19, 25 (S.D.N.Y. 1984) (Sofaer, J.) (quoting *Rey v. Penn Shipping Co.*, 277 F.2d 905, 906-907 (2d Cir. 1960), *cert. denied* 364 U.S. 829); *see also*

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[5] Although Sears owns no Dean Witter stock directly, it is the sole owner of Dean Witter Financial Services Inc., which is the sole owner of Dean Witter.

[6] Although Sears has captioned and styled its brief based on a third-party beneficiary theory, it does not press this theory vigorously. Instead, it quotes cases and directs its argument toward rearguing the motion for a stay which was previously denied. In essence, Sears has just put a new title on its previous motion.

Restatement (Second) of Contracts § 302(1) (1986). Under this test, Sears fails as an intended beneficiary. Although Sears may be an incidental beneficiary of the arbitration agreement, clearly the plaintiffs and Dean Witter did not make this contract to confer a direct benefit on Sears. *Chaplin v. Consolidated Edison Co. of New York*, 579 F. Supp. 1470, 1473 (S.D.N.Y. 1984) (Lasker, J.). Indeed, it is quite possible that the plaintiffs did not even know that Dean Witter was owned by Sears.

Furthermore, there is no evidence to suggest that Sears and Dean Witter are not distinct corporations in all respects. Therefore, Sears is merely a shareholder of Dean Witter and courts have recognized that generally a shareholder is an incidental, not intentional, beneficiary of a corporation's contract. *Sherman v. British Leyland Motors. Ltd.*, 601 F.2d 429, 440 n.13 (9th Cir. 1979); *Lait v. Leon*, 40 Misc.2d 60, 242 N.Y.S.2d 776, 781.

In sum, Sears' motion for a stay is denied.

IT IS SO ORDERED.

Dated: New York, New York
January 16, 1990

/s/ Robert L. Carter

Robert L. Carter
U.S.D.J.

IN THE UNITED STATES DISTRICT COURT FOR
THE EASTERN DISTRICT OF VIRGINIA
Richmond Division

HORACE D. McCOWAN, JR.
and
SARAH E. McCOWAN,

Plaintiffs,

v.

SEARS, ROEBUCK AND CO.,
a New York corporation,

Serve: Lewis Booker, Esquire
707 East Main Street
P.O. Box 1535
Richmond, VA 23212
its registered agent,

CIVIL ACTION
No. 86-0825R

and

DEAN WITTER REYNOLDS INC.,
a Delaware corporation,

Serve: Edward R. Parker, Esquire
5511 Staples Mill Road
Richmond, VA 23228
its registered agent,

Defendants.

COMPLAINT

1. Plaintiffs, Horace D. McCowan, Jr. and Sarah E. McCowan, are, and were at all times relevant to this action, citizens of Virginia and residents of the City of Richmond, Virginia. The defendants, Sears, Roebuck and Co. ("Sears") and Dean Witter Reynolds Inc. ("DWR"), are corporations incorporated under

the laws of the state of New York and Delaware, respectively. Each defendant's principal place of business is located in a state other than Virginia, and each has offices and agents and does business within the Eastern District of Virginia, and elsewhere.

2. The matter in controversy exceeds the sum of $10,000.00, exclusive of interest and costs.

3. This Court has jurisdiction, and venue is proper in this District, pursuant to 28 United States Code, Sections 1332 and 1391(a).

4. Upon information and belief, at all relevant times Sears directly or indirectly controlled DWR within the meaning of the Securities Act of Virginia, Sections 13.1-501 *et seq.* of the Code of Virginia.

5. Early in 1985 plaintiffs established an "Active Assets Account", No. 043065 ("Account"), with DWR as their broker. This Account was represented and presented to plaintiffs by DWR as being a highly liquid type account, one, for instance, against which plaintiffs could cash checks up to the full amount of the Account's margin loan value. The Account included a non-discretionary securities account ("Securities Account") described to plaintiffs by DWR as being "a conventional Dean Witter margin account". By the end of February, 1985, the Securities Account contained securities reported by DWR to have an aggregate value of over $1,000,000.00, and during January and February plaintiffs deposited in the Account additional cash totaling $500,000.00.

6. During the period ending October 31, 1985 DWR generated over $2,000,000.00 in cash through numerous sales of shares from the Securities Account and used this cash and additional loans it placed against the net equity value of the Securities Account to sell other shares to plaintiffs.

7. During the months of February through October, 1985, without prior advice to or authority from plaintiffs, through numerous transactions as a principal for its own account, DWR

sold to plaintiffs numerous shares of several securities, including an aggregate of 219,000 shares of Hawkeye Bancorp ("Hawkeye") and 120,000 shares of First Interstate of Iowa ("First Interstate") and as a part of each sale expressly or impliedly stated and represented to plaintiffs, among other things, that there then existed a "market" for such shares, that the shares had a determinable "market value" in that market, and that DWR as a "market maker" in the shares of Hawkeye and First Interstate stood ready and willing to repurchase these shares from plaintiffs for DWR's own account on a regular or continuous basis.

8. Each month DWR supplied plaintiffs with a statement of plaintiffs' Account. In each statement DWR reported and stated to plaintiffs the then number, "market value", current "portfolio value", and "net equity" value ("market value" less margin debt) of all shares of each and all securities then in the Securities Account, representing that each reported "market value" and its "portfolio valuation" were based upon an appraisal obtained by DWR from a quotation service.

9. In order to sell the shares of Hawkeye and First Interstate to plaintiffs as herein alleged, DWR sold other shares in plaintiffs' Securities Account as herein alleged and committed plaintiffs' cash funds and incurred substantial margin debt for plaintiffs in the Securities Account, all without prior advice to or authority from plaintiffs and without disclosure to plaintiffs until after the fact.

10. Other than stating that it was a "market maker" for such shares, in making such sales to plaintiffs DWR made no other disclosure of the extent to which it was interested in the shares of Hawkeye or First Interstate or was acting for its own interests rather than plaintiffs' interests.

11. As of June 30, 1985, DWR determined and reported to plaintiffs that the net equity value of the shares in the Securities Account then had reached $1,552,701.00, its highest reported value. In early November, however, when plaintiffs received

DWR's monthly statement (as of October 31, 1985) DWR reported that the then current net equity value of the shares in the Securities Account was only $1,025,170.00.

12. In its October 31, 1985 statement, DWR also stated and represented to plaintiffs that the shares of Hawkeye and First Interstate then held in the Securities Account then had a "portfolio value" of $1,587,750.00 and $330,000.00 respectively.

13. On receipt of the October statement, acting principally because of the decline in the reported net equity value of the shares in the Securities Account and the large margin debt, plaintiffs immediately directed DWR in writing to liquidate the shares in the Securities Account and to transfer control of the Account to DWR's Richmond, Virginia office.

14. Although authorized and directed by plaintiffs in early November to liquidate the Securities Account and sell its shares, DWR did not complete liquidation of Hawkeye and the Securities Account until January of 1986.

15. Upon DWR's eventual liquidation of the shares in the Securities Account and payment of all margin debt and costs the net return to plaintiffs was $294.01.

16. Upon information and belief, at all relevant times DWR was entirely familiar with and had peculiarly within its knowledge or available to it extensive, current, and material information concerning the shares of Hawkeye and First Interstate and their issuers and of the condition of the prevailing market in and for such shares, including, without limitation, information concerning each, any, or all of the following:

(a) the relative risks to a buyer in any sale of such shares by DWR, especially a sale on margin, and DWR's knowledge as to the advisability, nature, and extent of those risks;

(b) each fact bearing on the relative liquidity of such shares, including, without limitation, the extent to which such shares were, or were thought by DWR to be, relatively unmarketable;

(c) the absolute and relative size of DWR's position in such shares (long or short), the volume of such shares being offered and sold in the market being made for such shares by DWR and others, and the degree of concentration of the ownership, purchases, or sales of such shares, and

(d) those facts known to DWR that might affect, or that it believed might affect, share prices available in the market for such shares, including relevant information concerning the trades (or DWR's position in the trades) then being made in that market, the number and financial resources of the market makers participating with DWR, the volume of shares each market maker was offering to purchase or sell from time-to-time, and the prices being asked or offered for such shares in that market.

17. In connection with its sales of shares to plaintiffs as herein alleged DWR made statements as hereinafter alleged in paragraphs 18 and 19 and additionally and alternatively failed to state material facts necessary in order to make the statements made by DWR as herein alleged, in the light of the circumstances under which they were made, not misleading, including a failure to make a full and fair disclosure to plaintiffs (a) of the use or intended use of plaintiffs' shares, cash, and margin, (b) of the extent to which DWR was interested in the shares of Hawkeye or First Interstate or in such sales or was acting for its own interests rather than plaintiffs' interests, (c) of all facts and opinions that DWR realized or should have realized would have or be likely to have a material bearing upon the desirability of the transactions from the viewpoint of plaintiffs, including any relevant opinions held by DWR as to the advisability of such transactions for plaintiffs, or (d) of each, any, or all of the material facts described in paragraphs 9 and 16 above.

18. Additionally and alternatively, while omitting to state to plaintiffs material facts it had a duty to state as herein alleged, DWR sold shares to plaintiffs as herein alleged by means of statements of facts as described in paragraphs 5, 7, and 8 and hereinabove, and also by expressly or impliedly stating or representing to plaintiffs that DWR (a) intended to and would

execute only authorized transactions on behalf of plaintiffs, (b) intended to and would deal fairly with and for plaintiffs, (c) intended to and would maintain the Securities Account in compliance with all rules and regulations of the Securities Exchange Commission, the Board of Governors of the Federal Reserve System, the New York Stock Exchange, and the National Association of Securities Dealers, Inc., as well as the policies of DWR, (d) was acting and would act only in the best interests of plaintiffs at all times, except as and to the extent otherwise fully and fairly disclosed to plaintiffs, (e) at all relevant times believed each material statement and representation set forth above to be true, and (f) had no knowledge of any fact or opinion material (or believed by DWR to be material) to any sale of shares herein alleged that it had not fully and fairly disclosed to plaintiffs so as not to mislead plaintiffs in the circumstances. Each such statement or representation by DWR to plaintiffs as herein alleged was material and untrue.

19. Additionally and alternatively, plaintiffs did not know of the untruths or omissions of DWR as herein alleged.

20. Additionally and alternatively, at all relevant times a fiduciary or similar relationship of trust and confidence existed between DWR and plaintiffs in connection with the sales of shares as herein alleged, and DWR was obligated, among other things, to fully and fairly disclose to plaintiffs (a) all facts that DWR knew, or should have known, were material (or that it thought were material) in connection with each sale of shares to or for plaintiffs as herein alleged and (b) each and all of the matters described in paragraphs 9, 16, and 17 above.

21. Additionally and alternatively, plaintiffs relied on each material statement or representation made by DWR as alleged in paragraphs 5, 7, 8, and 18 above, and DWR knew, or should have known, that each such statement or representation was untrue as herein alleged.

22. Additionally and alternatively, DWR acted with a reckless disregard of the consequences to others in making or permitting the statements and omissions herein alleged.

WHEREFORE, pursuant to Section 13.1-522(b) of the Code of Virginia, for DWR's violations of the provisions of Sections 13.1-522(a) and 13.1-502 of the Code of Virginia as herein alleged, plaintiffs demand judgment against the defendant Sears, only, in an amount equal to the consideration paid for the shares sold to plaintiffs by DWR as herein alleged together with interest thereon at the rate of six percent per annum, costs, and reasonable attorneys' fees, less the amount of any income received by plaintiffs on the shares, an amount exceeding $1,000,000.00.

Plaintiffs demand trial by jury.

HORACE D. McCOWAN
SARAH E. McCOWAN

By Counsel

Charles W. Laughlin
Christopher M. Malone
Alison J. Vadnais
Thompson & McMullan
100 Shockoe Slip
Richmond, VA 23219
Counsel for Plaintiffs

/s/ Charles W. Laughlin
Of counsel

(804) 649-7545

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

HORACE D. McCOWAN, JR. and SARAH E. McCOWAN,	:	
	:	87 Civ. 2336
Plaintiffs,	:	(RLC)
— against —	:	
SEARS, ROEBUCK AND CO., and DEAN WITTER REYNOLDS, INC.,	:	
Defendants.	:	

NOTICE OF APPEAL

Notice is hereby given that defendant Dean Witter Reynolds, Inc. hereby appeals to the United States Court of Appeals for the Second Circuit from the Order entered in this action on October 5, 1989.

Dated: November 6, 1989

MORGAN, LEWIS & BOCKIUS

By /s/ John Linsenmeyer
John Linsenmeyer
A Member of the Firm
Attorneys for Defendants
101 Park Avenue
New York, N.Y. 10178
(212) 309-6000

TO: Harry H. Wise III, Esq.
Attorney for Plaintiffs
329 West 89th Street
(Penthouse B)
New York, New York 10024

CERTIFICATE OF SERVICE

The undersigned hereby certifies that true and correct copies of the foregoing Notice of Appeal were served by first class mail, postage prepaid, on the following counsel of record on November 6, 1989:

Harry H. Wise III, Esquire
329 West 89th Street
Penthouse B
New York, NY 10024

Charles W. Laughlin, Esquire
Thompson & McMullan
100 Shockoe Slip
Richmond, VA 23219

/s/ Carol Davis

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

HORACE D. McCOWAN, JR. and SARAH E. McCOWAN,	:	
	:	87 Civ. 2336
Plaintiffs,	:	(RLC)
	:	
— against —	:	NOTICE OF MOTION FOR
SEARS, ROEBUCK AND CO., and DEAN WITTER REYNOLDS, INC.,	:	STAY PENDING ARBITRATION
Defendants.	:	

PLEASE TAKE NOTICE THAT, upon the complaint filed in *McCowan, et al. v. Sears, Roebuck and Co., et al.*, 87 Civ. 2336 (RLC) ("McCowan II"); the complaint and amended complaint filed in *McCowan, et al. v. Dean Witter Reynolds, Inc.*, 86 Civ. 8398 (RLC) ("McCowan I"); the written arbitration agreement between plaintiffs and defendant Dean Witter Reynolds, Inc. originally annexed as Exhibit A to the affidavit of John F. X. Peloso, sworn to on January 6, 1987, previously filed of record in McCowan I and attached hereto as Exhibit A; the affidavit of Richard F. Kotz, sworn to on January 30, 1987, and the affidavit of Erick R. Holt, sworn to on January 23, 1987, previously filed of record in McCowan II and attached hereto as Exhibits B and C, respectively; and all the pleadings and proceedings heretofore had in those two consolidated actions, defendant Sears, Roebuck and Co. will move this Court, at the United States Court House, Foley Square, New York City, before the Honorable Robert L. Carter on Friday, December 8, 1989 at 9:30 A.M., or as soon thereafter as counsel can be heard, for an Order pursuant to § 3 of the Federal Arbitration Act, 9 U.S.C. § 1, *et seq.*, staying the action in *Horace D.*

McCowan v. Sears, Roebuck and Co. and Dean Witter Reynolds, Inc., 87 Civ. 2336 (RLC), as against Sears, Roebuck and Co. pending arbitration of the claims against Sears, Roebuck and Co.

November 17, 1989

MORGAN, LEWIS & BOCKIUS

By: /s/ John Linsenmeyer
A Member of the Firm
Attorneys for Defendants
101 Park Avenue
New York, New York 10178
(212) 309-6000

TO: Charles W. Laughlin, Esq.
Thompson & McMullan
100 Shockoe Slip
Richmond, Virginia 23219
(804) 649-7545

Harry H. Wise III, Esq.
329 West 89th Street
Penthouse B
New York, New York 10024
(212) 759-9030

Attorneys for Plaintiffs

DEAN WITTER REYNOLDS INC.

CUSTOMER'S AGREEMENT

Gentlemen:

In consideration of your accepting one or more accounts of the undersigned (whether designated by name, number or otherwise) and your agreeing to act as brokers for the undersigned in the purchase or sale of securities or commodities, the undersigned agrees as follows:

1. All transactions under this agreement shall be subject to the constitution, rules, regulations, customs and usages of the exchange or market, and its clearing house, if any, where the transactions are executed by you or your agents, and, where applicable, to the provisions of the Securities Exchange Act of 1934, the Commodities Exchange Act, and present and future acts amendatory thereof and supplemental thereto, and the rules and regulations of the Federal Securities and Exchange Commission, the Board of Governors of the Federal Reserve System and of the Secretary of Agriculture in so far as they may be applicable.

2. Whenever any statute shall be enacted which shall affect in any manner or be inconsistent with any of the provisions hereof, or whenever any rule or regulation shall be prescribed or promulgated by the New York Stock Exchange, the Federal Securities and Exchange Commission, the Board of Governors of the Federal Reserve System and/or the Secretary of Agriculture which shall affect in any manner or be inconsistent with any of the provisions hereof, the provisions of this agreement so affected shall be deemed modified or superseded, as the case may be, by such statute, rule or regulation, and all other provisions of the agreement and the provisions as so modified or superseded, shall in all respects continue and be in full force and effect.

3. Except as herein otherwise expressly provided, no provision of this agreement shall in any respect be waived, altered, modified or amended unless such waiver, alteration, modification or amendment be committed to writing and signed by a member of your organization.

4. All monies, securities, commodities or other property which you may at any time be carrying for the undersigned or which may at any time be in your possession for any purpose, including safekeeping, shall be subject to a general lien for the discharge of all obligations of the undersigned to you, irrespective of whether or not you have made advances in connection with such securities, commodities or other property, and irrespective of the number of accounts the undersigned may have with you.

5. All securities and commodities or any other property, now or hereafter held by you, or carried by you for the undersigned (either individually or jointly with others), or deposited to secure the same, may from time to time and without notice to me, be carried in your general loans and may be pledged, re-pledged, hypothecated or re-hypothecated, separately or in common with other securities and commodities or any other property, for the sum due to you thereon or for a greater sum and without retaining in your possession and control for delivery a like amount of similar securities or commodities.

6. Debit balances of the accounts of the undersigned shall be charged with interest, in accordance with your usual custom, and with any increase in rates caused by money market conditions, and with such other charges as you may make to cover your facilities and extra services.

7. You are hereby authorized, in your discretion, should the undersigned die or should you for any reason whatsoever deem it necessary for your protection, to sell any or all of the securities and commodities or other property which may be in your possession or which you may be carrying for the undersigned (either individually or jointly with others), or to buy in any securities, commodities or other property of which the account or accounts of the undersigned may be short, or cancel any outstanding orders in order to close out the account or accounts of the undersigned in whole or in part or in order to close out any commitment made in behalf of the undersigned. Such sale, purchase or cancellation may be made according to your judgment and may be made, at your discretion, on the exchange or other market where such business is then usually transacted, or at

public auction or at private sale, without advertising the same and without notice to the undersigned or to the personal representatives of the undersigned, and without prior tender, demand or call of any kind upon the undersigned or upon the personal representatives of the undersigned, and you may purchase the whole or any part thereof free from any right of redemption, and the undersigned shall remain liable for any deficiency; it being understood that a prior tender, demand or call of any kind from you, or prior notice from you, of the time and place of such sale or purchase shall not be considered a waiver of your right to sell or buy any securities and/or commodities and/or other property held by you, or owed you by the undersigned, at any time as hereinbefore provided.

8. The undersigned will at all times maintain margins for said accounts, as required by you from time to time.

9. The undersigned undertakes, at any time upon your demand, to discharge obligations of the undersigned to you, or, in the event of a closing of any account of the undersigned in whole or in part, to pay you the deficiency, if any, and no oral agreement or instructions to the contrary shall be recognized or enforceable.

10. In case of the sale of any security, commodity, or other property by you at the direction of the undersigned and your inability to deliver the same to the purchaser by reason of failure of the undersigned to supply you therewith, then and in such event, the undersigned authorizes you to borrow any security, commodity, or other property necessary to make delivery thereof, and the undersigned hereby agrees to be responsible for any loss which you may sustain thereby and any premiums which you may be required to pay thereon, and for any loss which you may sustain by reason of your inability to borrow the security, commodity, or other property sold.

11. At any time and from time to time, in your discretion, you may without notice to the undersigned apply and/or transfer any or all monies, securities, commodities and/or other property

of the undersigned interchangeably between any accounts of the undersigned (other than from Regulated Commodity Accounts).

12. It is understood and agreed that the undersigned, when placing with you any sell order for short account, will designate it as such and hereby authorizes you to mark such order as being "short", and when placing with you any order for long account, will designate it as such and hereby authorizes you to mark such order as being "long". Any sell order which the undersigned shall designate as being for long account as above provided, is for securities then owned by the undersigned and, if such securities are not then deliverable by you from any account of the undersigned, the placing of such order shall constitute a representation by the undersigned that it is impracticable for him then to deliver such securities to you but that he will deliver them as soon as it is possible for him to do so without undue inconvenience or expense.

13. In all transactions between you and the undersigned, the undersigned understands that you are acting as the brokers of the undersigned, except when you disclose to the undersigned in writing at or before the completion of a particular transaction that you are acting, with respect to such transaction, as dealers for your own account or as brokers for some other person.

14. Reports of the execution of orders and statements of the accounts of the undersigned shall be conclusive if not objected to in writing, the former within two days, and the latter within ten days, after forwarding by you to the undersigned by mail or otherwise.

15. Communications may be sent to the undersigned at the address of the undersigned given below, or at such other address as the undersigned may hereafter give you in writing, and all communications so sent, whether by mail, telegraph, messenger or otherwise, shall be deemed given to the undersigned personally, whether actually received or not.

16. Any controversy between you and the undersigned arising out of or relating to this contract or the breach thereof, shall

be settled by arbitration, in accordance with the rules, then obtaining, of either the Arbitration Committee of the Chamber of Commerce of the State of New York, or the American Arbitration Association, or the Board of Arbitration of the New York Stock Exchange, as the undersigned may elect. If the undersigned does not make such election by registered mail addressed to you at your main office within five (5) days after receipt of notification from you requesting such election, then the undersigned authorizes you to make such election in behalf of the undersigned. Any arbitration hereunder shall be before at least three arbitrators and the award of the arbitrators, or of a majority of them, shall be final, and judgment upon the award rendered may be entered in any court, state or federal, having jurisdiction.

17. This agreement and its enforcement shall be governed by the laws of the State of New York and its provisions shall be continuous, shall cover individually and collectively all accounts which the undersigned may open or re-open with you, and shall enure to the benefit of your present organization, and any successor organization, irrespective of any change or changes at any time in the personnel thereof, for any cause whatsoever, and of the assigns of your present organization or any successor organization, and shall be binding upon the undersigned and/or the estate, executors, administrators and assigns of the undersigned.

18. The undersigned, if an individual, represents that the undersigned is of full age, that the undersigned is not an employee of any exchange, or of any corporation of which any exchange owns a majority of the capital stock, or of a member of any exchange, or of a member firm or member corporation registered on any exchange, or of a bank, trust company, insurance company or of any corporation, firm or individual engaged in the business of dealing, either as broker or as principal, in securities, bills of exchange, acceptances or other forms of commercial paper. The undersigned further represents that no one except the undersigned (and, to the extent community property stands in the account or accounts, his or her spouse)

has an interest in the account or accounts of the undersigned with you.

19. The undersigned acknowledges receipt of your statement of interest charges.

Dated: 11/17/84
Richmond, VA
(City) (State)

Very truly yours,

X /s/ Horace D. McCowan
Horace D. McCowan

X /s/ Sarah E. McCowan
Sarah E. McCowan

CUSTOMER'S LOAN CONSENT

Until you receive written notice of revocation from the undersigned, you are hereby authorized to lend, to yourselves as brokers or to others, any securities held by you on margin for the account of, or under the control of, the undersigned.

Dated: 11/17/84
Richmond, VA
(City) (State)

X /s/ Horace D. McCowan
Horace D. McCowan

X /s/ Sarah E. McCowan
Sarah E. McCowan

AFFIDAVIT

STATE OF ILLINOIS)

) s.s.:

COUNTY OF COOK)

RICHARD F. KOTZ, being duly sworn, deposes and says:

I am an Assistant Secretary of SEARS, ROEBUCK AND CO., a New York corporation ("Sears").

I am making this affidavit in connection with that certain action pending in the United States District Court for the Eastern District of Virginia, Richmond Division, styled, *Horace D. McCowan, Jr. and Sarah E. McCowan, Plaintiffs, versus Sears, Roebuck and Co. and Dean Witter Reynolds Inc., Defendants.*

On October 1, 1981, Sears acquired all of the authorized capital stock of Sears Acquisition Corporation, a Delaware corporation ("SAC"). On December 31, 1981, Dean Witter Reynolds Organization Inc., a Delaware corporation and the parent company of Dean Witter Reynolds Inc., was merged with and into SAC, and the name of SAC was changed to Dean Witter Reynolds Organization Inc. ("DWRO"). On October 13, 1982, the name of DWRO was changed to Dean Witter Financial Services Inc. ("DWFSI").

At all times during the period from December 31, 1981 through October 31, 1986, DWFSI was a wholly-owned subsidiary of Sears.

At all times during the period from December 31, 1981 through October 31, 1986, Dean Witter Reynolds Inc., a Delaware corporation ("DWR"), was a wholly-owned subsidiary of DWFSI.

I have made a review of the pertinent corporate books and records of Sears, and have determined that, at any time during

the period from January 1, 1986 through October 31, 1986: (1) the Boards of Directors of Sears, DWFSI and DWR have had only one member in common, and (2) no officers of Sears have served as officers of DWFSI or DWR.

/s/Richard F. Kotz
Richard F. Kotz

Sworn to before me this 30th
day of January, 1987.

/s/
Notary Public

My Commission Expires July 14, 1988.

AFFIDAVIT

STATE OF NEW YORK)

) s.s.:

COUNTY OF NEW YORK)

ERICK R. HOLT, being duly sworn, deposes and says:

I am an Assistant Secretary of DEAN WITTER REYNOLDS INC., a Delaware corporation ("DWR").

I am making this affidavit in connection with that certain action pending in the United States District Court for the Eastern District of Virginia, Richmond Division, styled, *Horace D. McCowan, Jr. and Sarah E. McCowan, Plaintiffs, versus Sears, Roebuck and Co. and Dean Witter Reynolds Inc., Defendants.*

On October 1, 1981, Sears, Roebuck and Co., a New York corporation ("Sears"), acquired all of the authorized capital stock of Sears Acquisition Corporation, a Delaware corporation ("SAC"). On December 31, 1981, Dean Witter Reynolds Organization Inc., a Delaware corporation and the parent company of DWR was merged with and into SAC, and the name of SAC was changed to Dean Witter Reynolds Organization Inc. ("DWRO"). On October 13, 1982, the name of DWRO was changed to Dean Witter Financial Services Inc. ("DWFSI").

At all times during the period from December 31, 1981 through October 31, 1986, DWFSI was a wholly-owned subsidiary of Sears.

At all times during the period from December 31, 1981 through October 31, 1986, DWR, was a wholly-owned subsidiary of DWFSI.

At any time during the period from January 1, 1985 through December 31, 1985, the Boards of Directors of each of DWFSI

and DWR had only one member in common with the Board of Directors of Sears.

/s/Erick R. Holt
Erick R. Holt

Sworn to before me this
day of January, 1987.

/s/
Notary Public

Patricia A. _____
Notary Public, State of New York
No. 31-_____
Qualified in New York County
Commission Expires July 31, 1988.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

HORACE D. McCOWAN, JR. and SARAH E. McCOWAN,	:	
Plaintiffs,	:	87 Civ. 2336 (RLC)
—against—	:	NOTICE OF APPEAL
SEARS, ROEBUCK AND CO., and DEAN WITTER REYNOLDS, INC.,	:	
Defendants.	:	

PLEASE TAKE NOTICE that defendant Sears, Roebuck and Co. hereby appeals to the United States Court of Appeals for the Second Circuit from the Order entered in this action on January 17, 1990.

January 24, 1990

MORGAN, LEWIS & BOCKIUS
By: /s/ John Linsenmeyer
John Linsenmeyer
A Member of the Firm
Attorneys for Defendants
101 Park Avenue
New York, N.Y. 10178
(212) 309-6000

TO: HARRY H. WISE III, ESQ.
329 West 89th Street
(Penthouse B)
New York, N.Y. 10024
(212) 724-1231
— and
CHARLES W. LAUGHLIN, ESQ.
Messrs. Thompson & McMullan
100 Shockoe Slip
Richmond, Virginia 23219
(804) 649-7545
Attorneys for Plaintiffs

and

CLERK,
Southern District
of New York

AFFIDAVIT OF SERVICE

STATE OF NEW YORK)
: ss.
COUNTY OF NEW YORK)

The undersigned, being duly sworn, deposes and says that he served the foregoing Notice of Appeal, via first class mail on Harry H. Wise, Esq., 329 West 89th Street (Penthouse B), New York, N.Y. 10024, and Charles W. Laughlin, Esq., Messrs. Thompson & McMullan, 100 Shockoe Slip, Richmond, Virginia 23219, attorneys for plaintiffs, on Wednesday, January 24, 1990.

/s/

Subscribed and sworn to
before me this 24th day
of January 1990

/s/Augusta M. Tarter
Notary Public

Augusta M. Tarter
Notary Public, State of New York
No. 31-4886429
Qualified in New York County
Commission Expires February 9, 1991

FEDERAL RULES OF APPELLATE PROCEDURE

Rule 3. Appeal as of Right—How Taken

(a) **Filing the Notice of Appeal.** An appeal permitted by law as of right from a district court to a court of appeals shall be taken by filing a notice of appeal with the clerk of the district court within the time allowed by Rule 4. Failure of an appellant to take any step other than the timely filing of a notice of appeal does not affect the validity of the appeal, but is ground only for such action as the court of appeals deems appropriate, which may include dismissal of the appeal. Appeals by permission under 28 U.S.C. § 1292(b) and appeals by allowance in bankruptcy shall be taken in the manner prescribed by Rule 5 and Rule 6, respectively.

(b) **Joint or Consolidated Appeals.** If two or more persons are entitled to appeal from a judgment or order of a district court and their interests are such as to make joinder practicable, they may file a joint notice of appeal, or may join in appeal after filing separate timely notices of appeal, and they may thereafter proceed on appeal as a single appellant. Appeals may be consolidated by order of the court of appeals upon its own motion or upon motion of a party, or by stipulation of the parties to the several appeals.

(c) **Content of the Notice of Appeal.** The notice of appeal shall specify the party or parties taking the appeal; shall designate the judgment, order or part thereof appealed from; and shall name the court to which the appeal is taken. Form 1 in the Appendix of Forms is a suggested form of a notice of appeal. An appeal shall not be dismissed for informality of form or title of the notice of appeal.

* * *

(Rule 3(a) amended April 25, 1989, eff. Dec. 1, 1989.)

Rule 4. Appeal as of Right—When Taken

(a) **Appeals in Civil Cases.**

(1) In a civil case in which an appeal is permitted by law as of right from a district court to a court of appeals the notice of appeal required by Rule 3 shall be filed with the clerk of the

district court within 30 days after the date of entry of the judgment or order appealed from; but if the United States or an officer or agency thereof is a party, the notice of appeal may be filed by any party within 60 days after such entry. If a notice of appeal is mistakenly filed in the court of appeals, the clerk of the court of appeals shall note thereon the date on which it was received and transmit it to the clerk of the district court and it shall be deemed filed in the district court on the date so noted.

(2) Except as provided in (a)(4) of this Rule 4, a notice of appeal filed after the announcement of a decision or order but before the entry of the judgment or order shall be treated as filed after such entry and on the day thereof.

(3) If a timely notice of appeal is filed by a party, any other party may file a notice of appeal within 14 days after the date on which the first notice of appeal was filed, or within the time otherwise prescribed by this Rule 4(a), whichever period last expires.

(4) If a timely motion under the Federal Rules of Civil Procedure is filed in the district court by any party: (i) for judgment under Rule 50(b); (ii) under Rule 52(b) to amend or make additional findings of fact, whether or not an alteration of the judgment would be required if the motion is granted; (iii) under Rule 59 to alter or amend the judgment; or (iv) under Rule 59 for a new trial, the time for appeal for all parties shall run from the entry of the order denying a new trial or granting or denying any other such motion. A notice of appeal filed before the disposition of any of the above motions shall have no effect. A new notice of appeal must be filed within the prescribed time measured from the entry of the order disposing of the motion as provided above. No additional fees shall be required for such filing.

(5) The district court, upon a showing of excusable neglect or good cause, may extend the time for filing a notice of appeal upon motion filed not later than 30 days after the expiration of the time prescribed by this Rule 4(a). Any such motion which

is filed before expiration of the prescribed time may be *ex parte* unless the court otherwise requires. Notice of any such motion which is filed after expiration of the prescribed time shall be given to the other parties in accordance with local rules. No such extension shall exceed 30 days past such prescribed time or 10 days from the date of entry of the order granting the motion, whichever occurs later.

(6) A judgment or order is entered within the meaning of this Rule 4(a) when it is entered in compliance with Rules 58 and 79(a) of the Federal Rules of Civil Procedure. ***

UNITED STATES CODE
TITLE 9

§ 3. Stay of proceedings where issue therein referable to arbitration

If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration.

July 30, 1947, c. 392, 61 Stat. 670.

* * *

§ 15. Appeals

(a) An appeal may be taken from—

(1) an order—

(A) refusing a stay of any action under section 3 of this title,

(B) denying a petition under section 4 of this title to order arbitration to proceed,

(C) denying an application under section 206 of this title to compel arbitration,

(D) confirming or denying confirmation of an award or partial award, or

(E) modifying, correcting, or vacating an award;

(2) an interlocutory order granting, continuing, or modifying an injunction against an arbitration that is subject to this title; or

(3) a final decision with respect to an arbitration that is subject to this title.

(b) Except as otherwise provided in section 1292(b) of title 28, an appeal may not be taken from an interlocutory order –

(1) granting a stay of any action under section 3 of this title;

(2) directing arbitration to proceed under section 4 of this title;

(3) compelling arbitration under section 206 of this title; or

(4) refusing to enjoin an arbitration that is subject to this title.

(Added Pub.L. 100-702, Title X, § 1019(a), Nov. 19, 1988, 102 Stat. 4671.)

CODE OF VIRGINIA ANNOTATED (1956)
("Virginia Securities Act")

§ 13.1-502. Unlawful offers and sales. — It shall be unlawful for any person in the offer or sale of any securities, directly or indirectly,

(1) To employ any device, scheme or artifice to defraud, or

(2) To obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) To engage in any transaction, practice or course of business which operates or would operate as a fraud or deceit upon the purchaser. (1956, c. 428.)

* * *

§ 13.1-522. Civil liabilities. — (a) Any person who:

(1) Sells a security in violation of § 13.1-502, § 13.1-504 (a), § 13.1-507, § 13.1-510 (e) or § 13.1-510 (f), or

(2) Sells a security by means of an untrue statement of a material fact or any omission to state a material fact necessary in order to make the statement made, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission,

Shall be liable to the person purchasing such security from him who may sue either at law or in equity to recover the consideration paid for such security, together with interest thereon at the rate of six percent per annum, costs, and reasonable attorneys' fees, less the amount of any income received on the security, upon the tender of such security, or for the substantial equivalent in damages if he no longer owns the security.

(b) Every person who materially participates or aids in a sale made by any person liable under subsection (a), or who directly or indirectly controls any person so liable, shall also be liable jointly and severally with and to the same extent as the person so liable, unless the person who so participates, aids or controls sustains the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of the existence of the facts by reason of which the liability is alleged to exist. There shall be contribution as in cases of contract among the several persons so liable.

(c) Any tender specified in this section may be made at any time before entry of judgment.

(d) No suit shall be maintained to enforce any liability created under this section unless brought within two years after the transaction upon which it is based; provided, that if any person liable by reason of subsection (a) or (b) makes a written offer, before suit is brought, to refund the consideration paid, together with

interest thereon at the rate of six percent per annum, less the amount of any income received on the security, or to pay damages if the purchaser no longer owns the security, no purchaser shall maintain a suit under this section who shall have refused or failed to accept such offer within thirty days of its receipt.

(e) Any condition, stipulation or provision binding any person acquiring any security to waive compliance with any provision of this chapter or of any rule or order thereunder shall be void.

(f) The rights and remedies provided by this chapter shall be in addition to any and all other rights and remedies that may exist at law or in equity.
(Code 1950, § 13-150; 1956, c. 428) (amended 1987).

FEDERAL RULES OF CIVIL PROCEDURE

Rule 8. General Rules of Pleading

(a) **Claims for Relief.** A pleading which sets forth a claim for relief, whether an original claim, counterclaim, cross-claim, or third-party claim, shall contain (1) a short and plain statement of the grounds upon which the court's jurisdiction depends, unless the court already has jurisdiction and the claim needs no new grounds of jurisdiction to support it, (2) a short and plain statement of the claim showing that the pleader is entitled to relief, and (3) a demand for judgment for the relief the pleader seeks. Relief in the alternative or of several different types may be demanded.

* * *

Rule 19. Joinder of Persons Needed for Just Adjudication

(a) **Persons to be Joined if Feasible.** A person who is subject to service of process and whose joinder will not deprive the court of jurisdiction over the subject matter of the action shall be joined as a party in the action if (1) in the person's absence complete relief cannot be accorded among those already parties, or (2) the person claims an interest relating to the subject of the action and is so situated that the disposition of the action in the

person's absence may (i) as a practical matter impair or impede the person's ability to protect that interest or (ii) leave any of the persons already parties subject to a substantial risk of incurring double, multiple, or otherwise inconsistent obligations by reason of the claimed interest. If the person has not been so joined, the court shall order that the person be made a party. If the person should join as a plaintiff but refuses to do so, the person may be made a defendant, or, in a proper case, an involuntary plaintiff. If the joined party objects to venue and joinder of that party would render the venue of the action improper, that party shall be dismissed from the action. * * *

(2)

No. 90-279

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

HORACE D. McCOWAN, JR. and
SARAH E. McCOWAN,
Petitioners

v.

SEARS, ROEBUCK & Co., and
DEAN WITTER REYNOLDS INC.,
Respondents

On Petition for Writ of Certiorari to the United States Court of Appeals for the Second Circuit

---

BRIEF OF RESPONDENTS SEARS, ROEBUCK & CO. AND DEAN WITTER REYNOLDS INC. IN OPPOSITION

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COUNTERSTATEMENT OF THE QUESTIONS PRESENTED

1. Where customers of a securities brokerage firm, in order to evade a valid and enforceable arbitration contract which they had signed, commenced different Federal Court lawsuits in two judicial districts, including one against the brokerage firm and another against the corporate grand-parent of the brokerage firm solely on a *respondeat superior* theory of vicarious liability for the alleged misdeeds of the brokerage firm, and where the Court of Appeals had undisputed jurisdiction over an appeal from the denial of a stay pending arbitration in the customers' lawsuit against the corporate grand-parent, but appellate jurisdiction over a closely-related appeal by the securities brokerage firm was disputed, was the Court of Appeals precluded from deciding identical issues raised in both appeals, particularly where (i) the decision of the issues in the corporate grand-parent's appeal (the action where alleged liability was entirely vicarious) required the Court of Appeals to determine the merits of all the issues raised by the other appeal, (ii) the two actions against the brokerage firm and its corporate grandparent had been consolidated prior to the appeal(s), and (iii) the District Court's denial of arbitration in the first appeal was clearly erroneous and inevitably would have required eventual reversal after protracted and totally pointless litigation?

2. Where those customers' efforts to evade their arbitration contract included multiple lawsuits arising out of identical transactions and facts, which thereby created a complex (and likely unique) procedural situation, and where the Court of Appeals acted to clarify that situation on the grounds that all the litigation arose from a single set of facts involving a single securities brokerage account and should be brought on for adjudication on the merits by the appropriate arbitral forum, and where no conflicts among the judicial circuits, no constitutional is-

sues and no questions of general public importance are alleged by the customers (who merely claim that the Court of Appeals acted unwisely or incorrectly), has any basis been shown upon which to grant a writ of certiorari for further appellate review by this Court?

PARTIES TO THE PROCEEDING

A list of the parties below is contained in the Petition. The following is a statement of the parent companies and subsidiaries (except wholly owned subsidiaries) of each corporation that is a party, provided pursuant to Rule 29.1 of this Court's Rules:

Sears, Roebuck & Co.; Dean Witter Financial Services Inc.; Dean Witter Reynolds Inc.; 134245 Canada Limited; Allstate Automobile & Fire Insurance Company Limited; Arden Fair Associates; Bay City Mall Associates; Carrefour Richelieu Realties Limited; Chandler Mall Associates; Chatham Centre Mall Limited; Citrus Park Venture; East Mesa Land Partnership; Hamden Mall Associates; H. Co. May Centers; H-D Lakeland Mall J.V.; H-D Pembroke J.V.; H-L Land Improvement Venture; H-L Mall Venture; H-L Office Venture; Hot Springs Mall Associates; Kelfor Holdings Limited; The Mall at Buckland Hills Partnership; New Park Associates; North 400 Venture; Prodigy Services; Regional Shopping Centres Limited; Saison Life Insurance Company, Ltd.; Samshin Allstate Life Insurance Company, Ltd.; Simon Homart San Antonio Mall Partnership; Simon Homart Shavano Partnership; Spring Creek Mall Associates; St. Laurent Centre (Partnership); Tires Plus Co.; Vista Ridge Joint Venture; Westgate Associates; The Woodlands Mall Assoc.

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On Petition for Writ of Certiorari to the United States Court of Appeals for the Second Circuit

---

BRIEF OF RESPONDENTS SEARS, ROEBUCK & CO. AND DEAN WITTER REYNOLDS INC. IN OPPOSITION

Respondents Sears, Roebuck & Co. ("Sears") and Dean Witter Reynolds Inc. ("Dean Witter") respectfully submit this Brief in opposition to the Petition of Horace D. McCowan, Jr. and Sarah E. McCowan (collectively "the McCowans") for a writ of certiorari to review the decision of the United States Court of Appeals for the Second Circuit in this case. The opinion of the Court of Appeals is not yet reported, but is provided in the Appendix to the Petition ("P. App.").

STATEMENT OF THE CASE

The McCowans claim that they lost money in a securities trading account by reason of non-disclosure and other misconduct by Dean Witter (P. App. at 62-66). Dean Witter and the McCowans had agreed in writing that "any controversy" between them would "be settled by arbitration" (P. App. at 75-76). All the lawsuits, appeals, orders, and various reported and unreported decisions of two District Courts and the Second Circuit, and the entire unique procedural tangle now presented to this Court, are the results of four years of increasingly frenzied effort by the McCowans to avoid arbitration notwithstanding this Court's decisions in *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220 (1987), and *Dean Witter Reynolds Inc. v. Byrd*, 470 U.S. 213 (1985).

The McCowans filed two District Court actions in 1986. The first (*"McCowan I"*, to use the Court of Appeals' terminology, *see* P. App. at 3) was commenced against Dean Witter only in the Southern District of New York and made claims under RICO, 18 U.S.C. § 1961, *et seq.*, and the Federal securities laws [2] that the transactions in their brokerage account with Dean Witter were unauthorized and that misrepresentations had been made by Dean Witter regarding their account. The second (*"McCowan II"*), a diversity case from which this Petition arises, was commenced in the Eastern District of Virginia, named both Dean Witter and Sears as defendants, and alleged that Dean Witter violated the antifraud provisions of the Securities Act of Virginia, Va. Code Ann. § 13.1-501, *et seq.* ("the Virginia Act"), in connection with transactions made in the McCowans' Dean Witter account in 1985 (P. App. at 61-67, 87-89). The complaint requested no relief against Dean Witter, but rather demanded "judgment against the defendant

[1] Claims were asserted under both the Securities Act of 1933 ("the Securities Act"), 15 U.S.C. § 77a, and the Securities Exchange Act of 1934 ("the Exchange Act"), 15 U.S.C. § 78a.

Sears, only," for damages for Dean Witter's alleged conduct (P. App. at 67) on the theory that Sears is a controlling person of Dean Witter under the Virginia Act and vicariously liable for Dean Witter's alleged violations of the statute.

The District Court in Virginia transferred *McCowan II* to the Southern District of New York, where it was consolidated with *McCowan I* already filed in that District in October 1986; *McCowan I* was based on the exact same transactions in the same brokerage account at issue in *McCowan II*.

In June 1987, Dean Witter and Sears filed a motion to dismiss *McCowan II* on the grounds that no relief was sought against Dean Witter, that the claims against Sears failed to state a claim for controlling person liability, and that the entire complaint failed to plead fraud with the required particularity. Alternatively, Dean Witter sought a stay pending arbitration under the Federal Arbitration Act, 9 U.S.C. § 3 (P. App. at 86).[2] At the time the motion was filed to dismiss or stay *McCowan II*, Dean Witter's motion to dismiss or stay *McCowan I* was already pending in the Southern District.

The District Court ruled on the motions to dismiss *McCowan I* and *McCowan II* in a decision issued in December 1987 and held that the arbitration provision in the customer's agreement between Dean Witter and the McCowans was valid, stayed the RICO and Exchange Act claims pending arbitration as required by this Court's decision in *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220 (1987), and dismissed the Securities Act claims with leave to replead. *McCowan v. Dean Witter Reynolds Inc.*, 682 F. Supp. 741 (S.D.N.Y. 1987). The District Court deferred ruling on the motion to dismiss the Virginia state law claim against Sears in *McCowan*

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[2] The arbitration clause in the McCowans' customer's agreement with Dean Witter is reproduced in P. App. at 75-76.

II pending the repleading of the Securities Act claims, and did not reach Dean Witter's alternative motion for a stay pending arbitration of *McCowan II*. *Id.* at 745.

The McCowans subsequently filed an amended complaint in *McCowan I* repleading their Securities Act claims, which was dismissed on Dean Witter's motion in April 1989 for failure to state a claim. *McCowan v. Dean Witter Reynolds Inc.*, 1989 Fed. Sec. L. Rep. (CCH) ¶ 94,423 (S.D.N.Y. April 12, 1989). The only other claims asserted in *McCowan I* had been stayed pending arbitration by the District Court's decision of December 1987. The McCowans appealed the orders dismissing the Securities Act claims and staying *McCowan I* pending arbitration of the RICO and Exchange Act claims; the Court of Appeals dismissed that appeal for lack of appellate jurisdiction since orders staying litigation pending arbitration are not immediately appealable. *McCowan v. Dean Witter Reynolds Inc.*, 889 F.2d 451 (2d Cir. 1989).

As of June 1989, all the *McCowan I* claims (*i.e.*, all the claims for relief against Dean Witter) that had not been dismissed had been stayed by the District Court pending arbitration, but the District Court had not ruled on the motion of Dean Witter and Sears to dismiss or stay *McCowan II*. As a consequence, Dean Witter and Sears filed a renewed motion to dismiss or, in the alternative, to stay *McCowan II*. Dean Witter requested a stay under § 3 of the Federal Arbitration Act, pending arbitration of the allegations that Dean Witter violated the Virginia Act. Sears moved for a discretionary stay of the state law claims asserted against it, pending arbitration of the matter as to Dean Witter. In that motion, Sears argued that the claim of controlling person liability should be dismissed for failure to state a claim, so Sears did not at that time seek to have the claim against it—the only claim for relief in *McCowan II*—referred to arbitration based upon the customer's agreement with Dean Witter.

On October 5, 1989, the District Court denied the motion to dismiss or stay *McCowan II* (P. App. at 39-53).[3] Dean Witter filed a motion for reconsideration under Local Rule 3(j) of the Southern District of New York, which was denied, and filed a Notice of Appeal on November 6, 1989.

Sears filed in November 1989 a motion under § 3 of the Federal Arbitration Act seeking a stay and referral of the Virginia Act claims against Sears to arbitration. Because the District Court had held in its October 1989 opinion that Sears is a controlling person of Dean Witter under the Virginia Act (P. App. at 46), Sears asserted its right to enforce the arbitration agreement because the McCowans' claims against Sears alleged only derivative and vicarious liability for the acts of Dean Witter. On January 17, 1990, the District Court denied Sears' motion for a stay under § 3 of the Federal Arbitration Act based solely on a finding that Sears was an incidental, rather than an intended, beneficiary of the customer's agreement between Dean Witter and the McCowans (P. App. at 56-60).

Sears filed a notice of appeal from the January 17, 1990 order on January 24, 1990, since interlocutory orders denying stays pending arbitration are immediately appealable under the Federal Arbitration Act, 9 U.S.C. § 15(a)(1)(A) (P. App. at 86). The appeal from the January 1990 decision denying Sears a stay pending arbitration was consolidated in the Court of Appeals with the appeal from the October 1989 decision denying Dean Witter a stay.

It is undisputed that the Court of Appeals had jurisdiction over the appeal from the January 1990 order denying Sears a stay under § 3 of the Federal Arbitra-

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[3] The District Court's opinion was filed October 5, 1989, although it is "dated" October 12, 1989, apparently a typographical error (P. App. at 53).

tion Act. With respect to the appeal from the October 1989 decision denying Dean Witter a stay, however, the Court of Appeals treated Dean Witter's motion for reconsideration as a motion under Rule 59(e) of the Federal Rules of Civil Procedure and regarded Dean Witter's Notice of Appeal as two days premature (P. App. at 10-11), conclusions with which Dean Witter disagrees but which have no direct bearing on the instant Petition. The Court of Appeals recognized nonetheless that the appeal from the January 1990 order as to Sears "requires analysis of the arbitration agreement entered into by the plaintiffs and Dean Witter" and an "examination of the relationship between the defendants and the basis upon which the plaintiffs assert liability against them" (P. App. at 13).

Emphasizing that no recovery against Sears as a controlling person is possible unless the McCowans first prove their contention that Dean Witter violated the Virginia Act (P. App. at 15), the Court of Appeals concluded that under § 3 of the Federal Arbitration Act the issue of whether Dean Witter violated the Virginia Act must be arbitrated in accordance with the arbitration clause in the customer's agreement (P. App. at 17). As a result, the Court of Appeals concluded that the claim for relief against Sears in *McCowan II*, which is wholly dependent on the allegations against Dean Witter, also could not proceed. The Court of Appeals stayed the entire *McCowan II* action pending arbitration (P. App. at 20).[4]

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[4] In December 1989, two years after the District Court stayed *McCowan I* pending arbitration of the RICO and Exchange Act claims, the McCowans filed a Demand for Arbitration with the American Arbitration Association asserting claims against Dean Witter under those statutes and for common law conversion and breach of contract. The case is scheduled to be heard by a panel of arbitrators in Richmond, Virginia on September 24, 1990 through September 28, 1990. A copy of the Notice of Hearing is provided in the Appendix to this Brief ("R. App.").

As this unduly convoluted matter now stands, all claims for relief against Dean Witter arising from the facts alleged in both *McCowan I* and *McCowan II* are to be arbitrated in several weeks. All claims for relief against Sears arising from the same facts—the *McCowan II* claims for relief—have been stayed at the direction of the Court of Appeals. In advance of the results of that arbitration (*see* R. App.), the McCowans ask this Court to review the Court of Appeals' interlocutory determination, apparently in an effort to litigate in the District Court their state law claims against Sears for the alleged misdeeds of Dean Witter, a litigation which can only reach a result after the McCowans' claims against Dean Witter have been decided on the merits by the arbitrators. In short, the McCowans seek relief which is simultaneously lacking in general importance (since the procedural snarl of *McCowan I and II* is hard to replicate), interlocutory, inefficient, and in all likelihood moot.

REASONS FOR DENYING THE WRIT

This case does not raise issues appropriate for the exercise of this Court's discretionary review by certiorari. It does not present any conflict between a decision of this Court and the decision of the Court of Appeals, or any conflict between decisions of several courts of appeals. Nor does it raise any important question of constitutional or federal law. The sole significant issue, *viz.*, whether the McCowans are bound by their arbitration contract no matter how much they object or how many times they sue or appeal, has already been decided in *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220 (1987), and *Dean Witter Reynolds Inc. v. Byrd*, 470 U.S. 213 (1985).

In reviewing the interlocutory order denying Sears a stay pending arbitration, where Sears' right to arbitration is dependent on Dean Witter's right to arbitration, the Court of Appeals was required to determine whether the

underlying claim against Dean Witter is subject to arbitration and correctly did so. The unique procedural posture of the case and the unusual position of Sears and Dean Witter as defendants and respondents—circumstances created by the McCowans' litigation strategies to evade their arbitration contract—suggest no reason for review by this Court and indeed weigh against the granting of interlocutory review of this exceptionally fact-bound matter.

I. THE COURT OF APPEALS HAD JURISDICTION OVER THE SEARS APPEAL AND IN HEARING THAT APPEAL WAS REQUIRED TO DETERMINE WHETHER THE ARBITRATION CLAUSE IN THE DEAN WITTER CUSTOMER AGREEMENT WAS VALID AND WHETHER THE CLAIMS BROUGHT UNDER THE VIRGINIA SECURITIES ACT FALL WITHIN THE SCOPE OF THAT ARBITRATION CLAUSE

The Petition focuses almost exclusively on the appeal from the October 1989 decision denying Dean Witter a stay under the Federal Arbitration Act, and ignores the fact that in the Sears appeal, as to which no jurisdictional issue exists, it was necessary for the Court of Appeals to determine whether the underlying dispute between the McCowans and Dean Witter is arbitrable. In other words, review of the order denying Sears a stay under § 3 of the Arbitration Act required a determination as to whether the arbitration clause in the customer's agreement with Dean Witter is enforceable and whether the Virginia state law claims asserted in this action fall within the scope of that arbitration clause. *See Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 626, 630 (1985). *See also Genesco, Inc. v. T. Kakiuchi & Co.*, 815 F.2d 840, 844 (2d Cir. 1987) (citing *Mitsubishi*).

The McCowans assert that the issues of whether Dean Witter and Sears are each entitled to stays are "totally

independent if not exclusive of each other" (Pet. at 8). This simply ignores the long line of cases holding that a non-signatory who is alleged to be vicariously or derivatively liable for the actions of a signatory to an arbitration agreement may be bound by, and may enforce, the arbitration proviso. Thus, for example, where there is an agency relationship between the signatory and the non-signatory, the non-signatory may enforce or be bound by the arbitration agreement. *See, e.g., Interbras Cayman Co. v. Orient Victory Shipping Co.*, 663 F.2d 4, 6 (2d Cir. 1981); *In re Oil Spill by the Amoco Cadiz*, 659 F.2d 789, 796 (7th Cir. 1981). Similarly, where a parent company or shareholder exercises control over the signatory so as to be an "alter-ego" or to justify piercing the corporate veil, the non-signatory parent or shareholder can both enforce and be bound by the arbitration agreement. *See, e.g., Farkar Co. v. R. A. Hanson DISC, Ltd.*, 583 F.2d 68, 70-71 (2d Cir. 1978); *Fisser v. Int'l Bank*, 282 F.2d 231, 234-35 (2d Cir. 1960). Whatever legal theory is relied upon to give the non-signatory the benefit or obligation of the arbitration agreement, the reasoning is the same: having sought to hold the non-signatory vicariously liable for damages for the actions of the signatory, the plaintiff cannot deny the non-signatory the benefit of the arbitration agreement. *See J.J. Ryan & Sons, Inc. v. Rhone Poulenc Textile, S.A.*, 863 F.2d 315, 320-21 (4th Cir. 1988). *See also McBro Planning & Dev. Co. v. Triangle Elec. Constr. Co.*, 741 F.2d 342, 344 (11th Cir. 1984); *In re Oil Spill by the Amoco Cadiz*, 659 F.2d at 796.

This line of authority is not, as suggested by the McCowans (Pet. at 10-11), inconsistent with the principle that parties cannot be required to arbitrate absent an agreement to do so, but rather relies on basic common law notions to determine when principals, parent corporations, and others alleged to be vicariously liable for the conduct of their agents and subsidiaries can be bound by, and enforce, arbitration agreements entered into by

the entities for whose conduct they are being held responsible: the "variety of ways in which a [non-signatory] . . . may become bound . . . is limited only by generally operative principles of contract law." *Fisser v. Int'l Bank*, 282 F.2d at 233.

For the McCowans to urge this Court (Pet. at 10) to grant the Petition on grounds that the decision of the Court of Appeals "directly conflicts with this Court's reasoning and comments in *Volt*, 109 S. Ct. at 1254 n.5" is captious. That footnote 5 in *Volt Information Sciences, Inc. v. Board of Trustees*, 109 S. Ct. 1248 (1989), merely observes that the Federal Arbitration Act "itself contains no provision designed to deal with the special practical problems that arise in multiparty contractual disputes when some or all of the contracts at issue include agreements to arbitrate." Similarly, that portion of the decision in *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, 460 U.S. 1 (1983), alleged (Pet. at 10) to be contradicted by the Court of Appeals' decision, holds only that an independent architectural firm hired to oversee a construction project cannot be required to arbitrate without its consent where the only arbitration clause is in a contract between the project owner and the general contractor. 460 U.S. at 4, 19-20. Neither point is significant in this case where a parent corporation, which is alleged only to be vicariously liable for the conduct of its subsidiary, seeks to enforce for its own benefit an arbitration clause in its subsidiary's contract with the plaintiff.

II. APPELLATE JURISDICTION WAS PROPERLY EXERCISED

The rubrics of pendent appellate jurisdiction and the scope of interlocutory appellate review are frequently treated as interchangeable and described in imprecise language; Professors Charles Alan Wright and Arthur Miller begin their commentary on "pendent and retained jurisdiction" with the observation that:

> A court of appeals may occasionally decide questions going beyond the obvious limits authorized by the appeal or petition before it. Many of the illustrations that might be offered involve nothing more than intelligent definition of the scope of interlocutory appeals, in light of the fact that the immediate occasion for appeal may warrant or even require consideration of closely related issues. . . .

16 C. Wright & A. Miller, *Federal Practice and Procedure* § 3937 (1977). They also observe that "jurisdiction of the interlocutory appeal is in large measure jurisdiction to deal with all aspects of the case that have been sufficiently illuminated to enable decision by the court of appeals without further trial court development." *Id.* at § 3921. *See Thornburgh v. American College of Obstetricians & Gynecologists*, 476 U.S. 747, 756-57 (1986); *Deckert v. Independence Shares Corp.*, 311 U.S. 282, 287 (1940); *Decker Coal Co. v. Commonwealth Edison Co.*, 805 F.2d 834, 837 n.1 (9th Cir. 1986); *Intermedics Infusaid, Inc. v. Regents of Univ. of Minnesota*, 804 F.2d 129, 134 (Fed. Cir. 1986); *Mansbach v. Prescott, Ball & Turben*, 598 F.2d 1017, 1023 (6th Cir. 1979); *Lee v. Ply*Gem Indus., Inc.*, 593 F.2d 1266, 1270 (D.C. Cir.), *cert. denied*, 441 U.S. 967 (1979); *McCreary Tire & Rubber Co. v. Ceat S.p.A.*, 501 F.2d 1032, 1037-38 (3d Cir. 1974).

In this case,[5] disposition of the Sears appeal, as to which there is no jurisdictional issue, required a determination of whether the arbitration agreement between the McCowans and Dean Witter is enforceable and whether the Virginia Act claims fall within the scope of that agreement.[6] Sears' right to a stay depends on the

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[5] It should be noted, although the McCowans pretend to forget, that "this case" includes both *McCowan I* and *McCowan II*, which were consolidated (P. App. at 3).

[6] Contrary to the arguments advanced in the Petition, there is no conflict or inconsistency between the Court of Appeals' necessary

enforceability and scope of Dean Witter's arbitration clause, and the Court of Appeals could not grant Sears full relief without determining whether Dean Witter was entitled to arbitration of the Virginia state law allegations. Had only Sears, and not Dean Witter, moved for a stay pending arbitration, or had Sears been the only defendant named in the case, an appeal from a denial of a stay as to Sears would have involved the same examination of the underlying issues as to Dean Witter. It hardly rises to the level appropriate for certiorari review to ask this Court to entertain this interlocutory matter simply to determine (i) whether as a matter of language or labelling the Court of Appeals exercised pendent appellate jurisdiction, or (ii) whether the Court of Appeals merely recognized that the scope of review as to Sears necessarily included consideration of all those fully briefed issues on which Sears' rights depend, and having performed that review, decided to correct a plain and closely-related error and to remand Dean Witter to arbitration before, rather than after, a long lawsuit and trial.

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determination of the issue regarding Dean Witter's arbitration agreement with the McCowans, and the decisions in *Abney v. United States*, 431 U.S. 651 (1977), that where a district court's rejection of a criminal defendant's double jeopardy claim is immediately reviewable under the narrow "collateral order" exception to the final judgment rule, other grounds for dismissal of the case rejected by the district court are reviewable at that time only if they satisfy the requirements of the "collateral order" exception, or in *Torres v. Oakland Scavenger Co.*, 487 U.S. 312 (1988), where the appeal of one of sixteen appellants was barred because due to a clerical error his name did not appear on the notice of appeal.

III. THE COURT OF APPEALS REACHED THE CORRECT RESULT IN STAYING YEARS OF LITIGATION DESIGNED SOLELY TO DENY BOTH DEAN WITTER AND SEARS THEIR STATUTORY AND CONTRACTUAL RIGHTS TO ARBITRATION

The Court of Appeals reached the correct result in staying this entire action pending arbitration of the McCowan's claims under the Virginia Act. The Petition does not purport to challenge the validity of the arbitration clause, or to contend that the Virginia Act claims are otherwise not subject to arbitration.[7]

Rather, the McCowans insist in the Petition that because they request no damages from named defendant Dean Witter in *McCowan II*, they have no "claim" against named defendant Dean Witter under the Virginia Act and therefore no "claim" to refer to arbitration. (Pet. at 8-9). The Court of Appeals cut through these semantics, observing:

> Although fashioned as two separate lawsuits, there is in reality a single "controversy" at issue—as that term would have been understood by the contracting parties—giving rise to claims under three separate laws: the 1934 Act, RICO and the Virginia Securities Act. The first two demand a money judgment from Dean Witter; the third requires a showing of liability against Dean Witter as a predicate to recovery against Sears, but demands no monetary judgment from Dean Witter (P. App. at 17).

The arbitration clause requires arbitration of "any controversy" (P. App. at 75), and § 3 of the Federal Arbitration Act speaks of arbitrable issues, not claims for relief, and requires that courts stay litigation pending arbitration "if any suit . . . be brought . . . upon any

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[7] The state law claims are not in any respect exempt from arbitration. *Dean Witter Reynolds Inc. v. Byrd*, 470 U.S. 213 (1985); *Newcome v. Esrey*, 659 F. Supp. 100, 104 (W.D.Va. 1987), *aff'd*, 862 F.2d 1099 (4th Cir. 1988).

issue referable to arbitration under an agreement in writing for such arbitration." 9 U.S.C. § 3 (emphasis added) (P. App. at 86).

This Court has recognized that the congressional intent underlying the Federal Arbitration Act includes an intent "to move the parties to an arbitrable dispute out of court and into arbitration as quickly and easily as possible." *Moses H. Cone Memorial Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 22 (1983). In directing that this entire case be stayed pending arbitration, the Court of Appeals sought to conclude an effort of nearly four years by the McCowans to avoid arbitration. Indeed, counsel for the McCowans acknowledged at oral argument in the Court of Appeals that the reason for the multiple actions was to attempt to avoid arbitration of the Virginia state law claim.

No final judgment has been entered in either *McCowan I* or *McCowan II*; both cases are stayed pending arbitration. Following the issuance of an award in the *McCowan I* arbitration scheduled to be tried in this month, there will doubtless be further court proceedings when the parties attempt to confirm or vacate the award, leading to an appealable final judgment. All the issues raised and preserved by the McCowans, by Sears and by Dean Witter in the litigation can then be heard on appeal. There is no reason for this Court to grant review of this matter at what is, notwithstanding that the case was filed in 1986, an interlocutory and preliminary stage in the litigation.

CONCLUSION

For these reasons, respondents urge that the Petition for Writ of Certiorari be denied.

Respectfully submitted,

JOHN LINSENMEYER *
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* Counsel of Record

APPENDIX

APPENDIX

APPENDIX

Notice of Hearing Before
American Arbitration Association

AMERICAN ARBITRATION ASSOCIATION

Case Number: 16 136 00674 89G

IN THE MATTER OF THE ARBITRATION BETWEEN
HORACE D. MCCOWAN, JR., & SARAH E. MCCOWAN

AND

DEAN WITTER REYNOLDS INC.

NOTICE OF HEARING

Charles W. Laughlin, Esq.	Robert E. Payne
Thompson & McMullan	McGuire, Woods, Battle,
100 Shockoe Slip	& Boothe
3rd Floor	One James Center
Richmond, VA 23219	Richmond, VA 23219

Please Take Notice that a Hearing in the above-entitled Arbitration will be held at the Arbitration Tribunal of the American Arbitration Association.

AT:	Richmond, Virginia—To Be Determined
DATE:	September 24-28, 1990
TIME:	10:00 am
BEFORE:	Morris G. Sahr William H. Malloy, Jr., Esq. John P. Connolly, Esq.

Please attend promptly with your witnesses and be prepared to present your proofs.

Jay Gordon
Case Administrator

Dated: May 30, 1990

NOTICE: The Arbitrator(s) have arranged their schedule and reserved the above date to meet the convenience of the Parties. Therefore, every effort should be made to appear on the date scheduled. In the event that unforeseen circumstances make it impossible to attend the hearing as scheduled, the Parties are to request a postponement no less than 48 hours before the time and date set for hearing. All requests for postponements must be communicated to the Case Administrator (not the Arbitrator). There should be no communication between Parties and the Arbitrator other than at oral hearings.

cc: Arbitrator(s)

Form 8-AAA-C-1/82